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No. ____

In the Supreme Court of the United States

THE BANK OF NEW YORK MELLON AND
THE BANK OF NEW YORK MELLON CORPORATION,
Petitioners,

v.

FREDERICK J. GREDE, AS TRUSTEE OF THE
SENTINEL LIQUIDATION TRUST,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

In *Caplin* v. *Marine Midland Grace Trust Co.*, 406 U.S. 416 (1972), this Court held that a bankruptcy trustee lacked standing to file claims against a third party on behalf of a select group of creditors where any recovery would go only to those creditors rather than to the estate. In the decision below, the Seventh Circuit held that the *Caplin* rule does not apply where such claims were assigned to a liquidation trustee even though, as in *Caplin*, any recovery would go only to the assigning creditors rather than to the estate. The Seventh Circuit expressly recognized that its ruling conflicts with *Williams* v. *California 1st Bank*, 859 F.2d 664, 665-667 (9th Cir. 1988). The question presented is:

Whether a trustee appointed by a bankruptcy court to liquidate the estate has the authority to pursue assigned creditor claims against a third party where any recovery will not go to the estate.

RULE 29.6 STATEMENT

The Bank of New York Mellon Corporation is the parent corporation of The Bank of New York Mellon f/k/a The Bank of New York. No publicly held corporation owns 10% or more of the Bank of New York Mellon Corporation's stock.

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PETITION FOR A WRIT OF CERTIORARI

Petitioners, The Bank of New York Mellon and The Bank of New York Mellon Corporation (collectively, "the Bank"), respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Seventh Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App., *infra*, 1a-8a) is reported at 598 F.3d 899. The district court's order (App., *infra*, 9a-25a) is reported at 409 B.R. 467.

JURISDICTION

The judgment of the court of appeals was entered on March 18, 2010. Petitioner's timely petition for rehearing en banc was denied on April 16, 2010. App., *infra*, 26a-27a. On July 7, 2010, the time within which to file this petition was extended by Justice Breyer to August 16, 2010. This Court's jurisdiction rests on 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

"The trustee in a case under this title is the representative of the estate." 11 U.S.C. § 323(a).

"The trustee shall *** collect and reduce to money the property of the estate for which such trustee serves ***." 11 U.S.C. § 704(a)(1).

STATEMENT

A. The Sentinel Bankruptcy

Sentinel was an investment manager that filed for Chapter 11 bankruptcy in August 2007. Respondent Frederick J. Grede ("Grede") was appointed trustee of the Sentinel estate in the Chapter 11 proceeding, in which Sentinel customers and other entities asserted unsecured claims. The Bank was Sentinel's only secured creditor.

In October 2007, Grede sued Sentinel's principals, alleging that they had defrauded Sentinel and its customers. In March 2008, Grede filed an adversary proceeding against the Bank, claiming that it had facilitated the Sentinel principals' alleged fraud. The district court granted the Bank's motion to dismiss the Trustee's claims in part. *Grede* v. *Bank of New York*, 2009 WL 188460 (N.D. Ill. Jan. 27, 2009). The remaining claims in that action are pending.

In December 2008, the bankruptcy court confirmed a Chapter 11 plan ("Plan") that established a Liquidation Trust to liquidate the Sentinel estate. C.A. App. 57.[1] The Plan also provided for Grede's resignation as Chapter 11 Trustee and his simultaneous appointment as Liquidation Trustee. *Id.* at 87 § 6.3. According to the Plan, Grede would thereby "become the appointed representative of the Estate in accordance with Section 1123(b)(3) of the Bankruptcy

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[1] "Although the central purpose of Chapter 11 is to facilitate reorganizations rather than liquidations (covered generally by Chapter 7), Chapter 11 expressly contemplates liquidations." *Florida Dept. of Revenue* v. *Piccadilly Cafeterias, Inc.*, 128 S. Ct. 2326, 2330 n.2 (2008) (citing 11 U.S.C. § 1129(a)(11)).

Code." *Ibid.* In the Bankruptcy Court's order confirming the Plan, Grede as Liquidation Trustee was given "all powers afforded a trustee under the Bankruptcy Code and Rules." *Id.* at 419 ¶ 4.

The Plan established "a distinct tranche of the Liquidation Trust," which it designated "Tranche-P," to hold the "Non-Estate Claims" of Sentinel customers who assigned those claims to the Liquidation Trust. C.A. App. 91 § 6.12. These Non-Estate Claims were defined broadly to include potential claims against numerous entities, including the Bank and "all Entities that entered into transactions with Sentinel." *Id.* at 74-75. The Plan authorized Grede to "prosecute, settle, and release the Non-Estate Claims" (*id.* at 89 § 6.5(c)), specifying that Sentinel creditors who did not hold claims assigned to Tranche-P "will not receive any distribution on account of Tranche-P." *Id.* at 91 § 6.12. Many but not all of the Sentinel customer claims were assigned to Tranche-P.

The Plan also established a "Liquidation Trust Expense Fund" from which Grede and his retained professionals are to be compensated. C.A. App. 91-92 § 6.14, 94 § 6.21. The Liquidation Trust Agreement provides that Grede shall receive both "hourly-based compensation" and "contingency-based compensation" tied to recoveries obtained for the Liquidation Trust. *Id.* at 148.

B. District Court Proceedings

In April 2009, Grede brought this action on behalf of Sentinel customers who had assigned their claims against the Bank to Tranche-P. C.A. App. 7 ¶ 5. He raised essentially the same claims that he had raised previously against the Bank, but now on

behalf of only the assigning customers, with any recovery to go only to the assignors, not to the estate. *Id.* at 43-50 ¶¶ 148-68.[2]

The Bank moved to dismiss this action, contending that Grede lacks standing and that his claims are insufficient as a matter of law. The district court granted the Bank's motion, holding that Grede lacks standing and not reaching the Bank's additional grounds for dismissal.

District Judge Zagel explained that a precedent of this Court bars standing where a bankruptcy trustee pursues claims for money not owed to the estate. App., *infra*, 16a, citing *Caplin* v. *Marine Midland Grace Trust Co.*, 406 U.S. 416 (1972). The court refused Grede's request to create an exception where the trustee is an assignee of such claims because "he is still subject to the Code's requirement that he act for the benefit of the estate." *Id.* at 19a. Moreover, the court reasoned, allowing a trustee to pursue such non-estate litigation risks diminishing the assets available to the estate's creditors. *Ibid.* As the court put it, bankruptcy law does not permit a trustee "to bring claims for the benefit of the few at the expense of the many." *Ibid.* Allowing Grede's claims to proceed would "essentially circumvent[] the order of priority of claims established by the Code" by distributing the proceeds solely to some holders of unsecured claims. *Id.* at 22a. For these and other reasons, the court concluded, "the estate has no interest in the claims, and Trustee has no authority under the Code to bring them." *Id.* at 21a-22a.

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[2] Pursuant to Rule 14(g)(ii), petitioner notes that respondent asserted diversity jurisdiction in the district court pursuant to 28 U.S.C. § 1332(a)(1).

C. The Court of Appeals' Decision

The Seventh Circuit reversed. It ruled that *Caplin* does not apply to a suit "by a liquidation trustee on assigned claims," likening the trust established to liquidate the estate to "a reorganized debtor." App., *infra*, 5a-6a.

The court of appeals rejected the Bank's contention that authorizing liquidation trustees to use estate assets to finance assigned litigation that will not benefit the estate creates a perverse incentive to free-ride off the estate in conflict with bankruptcy law principles. According to the panel, the Bank has no interest in avoiding such a harmful consequence. *Id.* at 7a.

The Seventh Circuit expressly recognized that its ruling conflicts with *Williams* v. *California 1st Bank*, 859 F.2d 664, 665-667 (9th Cir. 1988), opting instead for a contrary ruling in *Semi-Tech Litig., LLC* v. *Bankers Trust Co.*, 272 F. Supp. 2d 319, 323-324 (S.D.N.Y. 2003), aff'd, 450 F.3d 121 (2d Cir. 2006). The panel stated that "[w]e must choose between the second circuit's holding and the ninth's," and it chose the former. App., *infra*, 5a.[3]

REASONS FOR GRANTING THE PETITION

Grede was appointed Chapter 11 Trustee and then Liquidation Trustee for a specific purpose—to gather the Sentinel estate assets for distribution to Sentinel creditors in accordance with applicable

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[3] Although this Court used the term "standing" in *Caplin*, the Seventh Circuit expressed a preference for the term "authority" to avoid any confusion with Article III standing, which is not at issue in this case. App., *infra*, 3a. This petition uses the two terms interchangeably.

Bankruptcy Code provisions. He filed this lawsuit for a very different purpose—to obtain damages for a subset of Sentinel's unsecured creditors on their personal claims against the Bank. Far from maximizing the value of the estate, this lawsuit forces the estate to subsidize litigation that does not even purport to seek any benefit for the estate as a whole. Accordingly, Grede lacks authority to bring this lawsuit, and the Seventh Circuit's ruling should be vacated to ensure that bankruptcy estates are not used to bankroll litigation in which they have no interest.

The Seventh Circuit's ruling conflicts with *Caplin*, in which this Court held that a bankruptcy-court-appointed trustee lacks authority to pursue recoveries for select creditors rather than for the estate as a whole. The Seventh Circuit erred by allowing Grede to circumvent *Caplin* by means of a formalistic change of hats. As this Court said in *Caplin*, expanding a trustee's litigation authority is up to Congress, not the courts.

The decision below also conflicts with *Williams* v. *California 1st Bank*, 859 F.2d 664, 665-667 (9th Cir. 1988), as the Seventh Circuit expressly recognized. In *Williams*, the Ninth Circuit held that a liquidation trustee lacked authority to pursue assigned claims where any recoveries would go only to the assignor-creditors, not to the estate. Whereas the Ninth Circuit found the claims' assignment to the trustee an insufficient distinction from *Caplin* to require a different result, the Seventh Circuit agreed with the Second Circuit's view that such an assignment authorizes a trustee to pursue claims that, under *Caplin*, otherwise would be unauthorized. There is now a mature, three-way acknowledged conflict among the circuits.

The issue presented is one of exceptional importance. The longstanding rule that trustee litigation must seek to benefit the estate protects against free riding. The Seventh Circuit's abrogation of that rule when select creditor claims are assigned to a liquidation trustee will encourage wholesale assignments of such claims to liquidation trustees to enable the assignors to avoid the costs of litigation and instead foist them on the estate. The bankruptcy process was not designed for such an improper purpose. The need for clarity on this subject is critical for the proper administration of the soaring number of bankruptcy filings, especially in complex cases.[4]

I. THE RULING BELOW CONFLICTS WITH THIS COURT'S *CAPLIN* PRECEDENT AND THE PLAIN MEANING OF THE BANKRUPTCY CODE.

In *Caplin*, a "trustee in reorganization" appointed under Chapter X of the former Bankruptcy Act brought suit "for the benefit of a specific class of creditors, the debenture holders," against an indenture trustee charged with ensuring the sufficiency of the debtor's assets. 406 U.S. at 416, 421 n.12. The Court evaluated whether the trustee had standing by first looking to the statutory provisions governing the trustee's authority, where it found "nothing" that "enables him to collect money not owed to the es-

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[4] See *Bankruptcy Filings Highest Since 2006*, News Release, Administrative Office of the U.S. Courts (May 14, 2010), http://www.uscourts.gov/news/NewsView/10-05-14/Bankruptcy_Filings_Highest_Since_2006.aspx (bankruptcy filings rose 27% in last 12 months); Sara Murray, *Personal Bankruptcies Rise*, Wall St. J., Aug. 5, 2010, at A2.

tate." *Id.* at 428. Instead, under the plain language of the Act the trustee's task was "simply to 'collect and reduce to money the property of the estates.'" *Id.* at 428-429. Thus, a bankruptcy trustee lacked statutory authority to sue third parties for recoveries that would not go to the estate.

The Court then noted additional problems with such trustee suits: they would likely raise issues of subrogation, may be inconsistent with any independent actions brought by the affected creditors, and would not be as binding on all such creditors as a class action. 406 U.S. at 430-432 & n.22. The Court recognized that it would not necessarily be "unwise" to allow the trustee to bring such suits. *Id.* at 434. But it concluded that conferring standing on a trustee for such matters is "a policy decision [that] must be left to Congress and not to the judiciary." *Ibid.*

Congress responded to that invitation, when it replaced the Bankruptcy Act with the Bankruptcy Code in 1978, by considering and rejecting a proposal to broaden trustee litigation authority. The House bill included a proposed Section 544(c) which would have "overrule[d] *Caplin*" by authorizing both reorganization and liquidation trustees to sue for recoveries that would go only to select creditors "on whose rights the trustee has based the action." H.R. Rep. No. 95-595, at 370-371 (1977), 1978 U.S.C.C.A.N. 5963, 6326. That provision was dropped in conference. "The inability of the drafters of the Code to square the proposed § 544(c) with Rule 23 of the Federal Rules of Civil Procedure and the complex issues arising in class action situations led to a decision to delete the proposed subsection." Patrick A. Murphy & Eric E. Sagerman, CREDITORS' RIGHTS IN BANKRUPTCY § 13.7 (2d ed. 2009).

As a result, trustees were left with no greater litigation authority under the new Code than under the former Act. 124 Cong. Rec. H11,097 (Sept. 28, 1978); see *In re Ozark Restaurant Equip. Co.*, 816 F.2d 1222, 1227-1228 & n.9 (8th Cir. 1987) (describing history and applying the *Caplin* rule to Chapter 7 liquidation trustees). As numerous courts have recognized, Congress's affirmative rejection of this attempt to overrule *Caplin* maintained the enforceability of the *Caplin* rule on trustee standing under the new Code. *E.g.*, *DSQ Property Co.* v. *DeLorean*, 891 F.2d 128, 131 (6th Cir. 1989) ("The Bankruptcy Act still has no provision providing for a bankruptcy trustee to sue third parties on behalf of creditors"); *E.F. Hutton & Co.* v. *Hadley*, 901 F.2d 979, 986 (11th Cir. 1990) (*Caplin* "remain[s] the law under the revised bankruptcy statutes"); *In re Bradley*, 326 F. App'x 838, 839 (5th Cir. 2009). It is improper for courts to effect a change in the law that Congress specifically rejected. "Congress is presumed to be aware of [a] judicial interpretation of a statute and to adopt that interpretation when it re-enacts a statute without change." *Forest Grove Sch. Dist.* v. *T.A.*, 129 S. Ct. 2484, 2492 (2009). That is especially true where, as here, the judicial change increases the likelihood of vexatious litigation. See *Stoneridge Inv. Partners* v. *Scientific-Atlanta, Inc.*, 552 U.S. 148, 162-163 (2008).

The Bankruptcy Code limits the scope of a trustee's authority to serving the estate. A trustee appointed by a bankruptcy court is "the representative of the estate" (11 U.S.C. § 323(a)), who shall "collect and reduce to money the property of the estate for which such trustee serves." *Id.* § 704(a) (made applicable to Chapter 11 proceedings by *id.* § 1106(a)(1)). See *CFTC* v. *Weintraub*, 471 U.S. 343, 352 (1985) (a

trustee "has the duty to maximize the value of the estate"); *Ohio* v. *Kovacs*, 469 U.S. 274, 284 n.12 (1985) (a trustee is "charged with the duty of collecting and reducing the property of the estate"). "Property of the estate" is defined as "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a). A trustee's duty to gather that property for the benefit of the estate cannot be reconciled with the initiation of private litigation on behalf of select creditors.

Caplin established a bright-line rule essential to the administration of the many complex bankruptcy cases facing federal courts. If any recovery would go to the estate, the trustee has authority to bring suit. *E.g.*, *In re Bogdan*, 414 F.3d 507, 514 (4th Cir. 2005). If any recovery would go only to assigning creditors rather than to the estate, the trustee does not have such authority. *E.g.*, *E.F. Hutton*, 901 F.2d at 986; *Ozark Restaurant*, 816 F.2d at 1229-1230.

That rule holds true even outside the ordinary bankruptcy context. Thus, in *Boston Trading Group* v. *Burnazos*, 835 F.2d 1504, 1514 (1st Cir. 1987) (Breyer, J.), the court held that a receiver appointed by a federal court to pursue claims on behalf of defunct commodity investment firms lacked standing to pursue claims on behalf of individual investors in the firms' commodity pools. Then-Judge Breyer explained that there was "no relevant distinction between *Caplin* and the case before us," requiring the First Circuit "to follow the Supreme Court case." *Id.* at 1515-1516. Accord *Marion* v. *TDI Inc.*, 591 F.3d 137, 148 (3d Cir. 2010); *Fleming* v. *Lind-Waldock & Co.*, 922 F.2d 20, 25 (1st Cir. 1990); see also *Florida Dept. of Ins.* v. *Chase Bank of Tex. Nat'l Ass'n*, 274 F.3d 924, 929-931 (5th Cir. 2001) (applying *Caplin* to

deny liquidator of insolvent insurer standing to pursue policyholders' claims).

The Seventh Circuit, too, should have followed *Caplin*. It is undisputed that any recovery from this lawsuit will go not to the estate for pro rata distribution to the creditors but instead only to a subset of Sentinel's unsecured creditors. App., *infra*, 11a. Moreover, Grede's fees and expenses incurred in prosecuting this lawsuit will be paid out of estate assets. C.A. App. 91-92 § 6.14. Thus, this litigation not only will not benefit the estate but also will affirmatively harm it. Accordingly, as the district court correctly ruled, Grede lacks authority to bring this action. [5]

The Seventh Circuit thought this case distinguishable from *Caplin* on the ground that Grede brought claims assigned to a liquidation trust established by a confirmed Chapter 11 plan, likening the trust to a reorganized debtor "just like the reorganized United Airlines." App., *infra*, 6a. But unlike a reorganized debtor, the Liquidation Trust is not a going concern that emerged from bankruptcy ready to stand on its own feet. It was not established to generate additional assets and revenues or incur additional liabilities as part of its post-emergence operations. Neither Grede nor anyone else contributed any new capital or financing to allow the debtor to

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[5] As Professor Dan Schechter commented after the decision below issued: "The result in this case seems to circumvent the decision by Congress in 1978 to ratify *Caplin*." Dan Schechter, *Liquidation Trustee is Empowered to Assert Claims Assigned by Estate's Creditors Against Third Party Tortfeasors*, Commercial Finance Newsletter (Apr. 5, 2010), available on Westlaw at 2010 COMFINNL 28.

"emerge" from bankruptcy. The trust is not a rehabilitated "business" in the ordinary meaning of that term but simply a mechanism to liquidate the estate, *i.e.*, gather the estate's assets for pro rata distribution to the estate's creditors. This conclusion is confirmed by the IRS regulations governing liquidation trusts established by Chapter 11 plans:

> An organization will be considered a liquidating trust if it is organized for the primary purpose of liquidating and distributing the assets transferred to it, and if its activities are all reasonably necessary to, and consistent with, the accomplishment of that purpose. A liquidating trust is treated as a trust for purposes of the Internal Revenue Code because it is formed with the objective of liquidating particular assets and *not as an organization having as its purpose the carrying on of a profit-making business.*

26 C.F.R. § 301.7701-4(d) (emphasis added).

Moreover, the Plan makes clear that establishment of the Trust would not expand Grede's authority beyond those he held as Chapter 11 Trustee. The estate was to remain in place, and Grede's task was to liquidate it according to Code priorities. Specifically, the Plan established the Liquidation Trustee as "representative of the Estate *in accordance with Section 1123(b)(3) of the Bankruptcy Code.*" C.A. App. 87 § 6.3 (emphasis added). Section 1123(b)(3) authorizes a trustee to enforce only claims or interests "belonging to the debtor or to the estate." Further, after confirmation "the Chapter 11 Case will remain open pending final order of the Bankruptcy Court closing the case and the Bankruptcy Court shall retain jurisdiction" for numerous listed purposes, including

"[t]o determine on a non-exclusive basis, any and all Causes of Action and Non-Estate Claims that have been transferred to the Liquidation Trust on the Transfer Date." C.A. App. 104 § 9.1(b). Similarly, the Confirmation Order provides that the Liquidation Trustee will have "all powers afforded a trustee under the Bankruptcy Code and Rules" (C.A. App. 419 ¶ 4), underscoring that Grede's powers are coextensive with those of a bankruptcy trustee.

In sum, the Plan by its terms did not reorganize the debtor and free it from Bankruptcy Court oversight; it simply established a vehicle to liquidate the estate with the same trustee at the wheel. Both before and after confirmation of the Plan, Grede's authority was limited to marshaling the debtor's assets for the benefit of the estate. See *Holywell Corp.* v. *Smith*, 503 U.S. 47, 52-53 (1992) (noting that the duties of a person appointed to liquidate a debtor pursuant to a confirmed plan do not differ whether he is characterized as a "trustee in a case under title 11," "receiver," or "assignee"). Yet, the Seventh Circuit seized on Grede's redesignation from Chapter 11 Trustee to Liquidation Trustee to expand his litigation authority, contrary to the command of *Caplin*. See *Torch Liquidating Trust* v. *Stockstill*, 2008 WL 696233, at *6 n.4 (E.D. La. Mar. 13, 2008) ("prior case law is explicit that Litigation Trusts such as Plaintiff do not have standing to pursue the direct claims of creditors"), aff'd on alternate grounds, 561 F.3d 377 (5th Cir. 2009).

The Seventh Circuit's reliance on a formalistic distinction between pre- and post-plan liquidation trustees would allow the *Caplin* rule—and the statutory provisions on which its rests—to be circumvented by simply giving the trustee a new name or

label, which would empower him broadly to pursue private claims at the expense of the bankruptcy estate. The petition should be granted to ensure that this Court's precedents are not cast aside based on artificial distinctions.

II. THE RULING BELOW DEEPENS A CIRCUIT SPLIT OVER TRUSTEE STANDING TO BRING ASSIGNED CLAIMS THAT WILL NOT BENEFIT THE ESTATE.

As the Seventh Circuit expressly recognized, its ruling in this case conflicts with that of the Ninth Circuit in *Williams* v. *California 1st Bank*, 859 F.2d 664 (9th Cir. 1988). App., *infra*, 5a.

In *Williams*, over 100 investors in a Ponzi scheme initiated by the debtor assigned their claims against a bank that allegedly facilitated the scheme to a Chapter 7 liquidation trustee. Noting that "*Caplin* and its progeny control this case," the Ninth Circuit ruled that the trustee lacked standing to pursue those claims. 859 F.2d at 666-667. The court rejected the notion that "the mere fact of assignment in order to allow the Trustee to pursue the claims for the creditors sufficiently distinguishes this case to allow of a different result." *Id.* at 666. The court explained that, notwithstanding the assignments, "the Trustee, as in *Caplin*, is attempting to 'collect money not owed to the estate.'" *Id.* at 667. The court concluded that "*no* trustee, whether a reorganization trustee as in *Caplin* or a liquidation trustee," may assert such claims, finding support in "Congress' express decision not to overrule *Caplin*." *Ibid.* (emphasis added).

The Seventh Circuit rejected the *Williams* decision in favor of *Semi-Tech Litig., LLC* v. *Bankers*

Trust Co., 272 F. Supp. 2d 319 (S.D.N.Y. 2003), aff'd, 450 F.3d 121 (2d Cir. 2006). The district court in *Semi-Tech* disagreed with *Williams* on the ground that a trustee-assignee is "no different" from any other assignee "outside the bankruptcy context." *Id.* at 323-324. The Second Circuit affirmed, adopting the district court's opinion "as the law of this Circuit." 450 F.3d at 123. Courts in the Second Circuit continue to maintain that *Caplin* does not limit a trustee's standing to pursue assigned claims even where any recoveries will go only to the assignors and not to the estate. See *Taberna Capital Mgmt., LLC* v. *Jaggi*, 2010 WL 1424002, at *3 (S.D.N.Y. Apr. 9, 2010).

In contrast, other courts have followed *Williams* and held that "[t]he rule articulated in *Caplin* holds true even in cases where a creditor has assigned her claims to a trustee or Trust." *Trenwick Am. Litig. Trust* v. *Ernst & Young, L.L.P.*, 906 A.2d 168, 191 (Del. Ch. 2006), aff'd sub nom. *Trenwick Am. Litig. Trust* v. *Billett*, 931 A.2d 438 (Del. 2007); accord *Mukamal* v. *Bakes*, 383 B.R. 798, 811-814 (S.D. Fla. 2007) (post-confirmation liquidation trustee lacked standing to pursue assigned claims), aff'd on other grounds, 2010 WL 1731775 (11th Cir. Apr. 30, 2010).

This Court should grant the petition to resolve this conflict on the recurring issue whether the simple assignment of claims to a trustee obviates the *Caplin* rule on trustee standing. The conflict should be resolved against an "assignment" exception to *Caplin*. As Professor Schechter has observed: "If *Caplin* can be circumvented by the simple expedient of executing an assignment, then it is limited to a very strange set of facts, *i.e.*, when a trustee tries to assert claims belonging to creditors who do not con-

sent to his behavior." Dan Schechter, *Where Creditors Have Executed Formal Assignments of Tort Claims, Liquidation Trustee as Assignee Has Standing to Prosecute Creditors' Claims*, Commercial Finance Newsletter (Apr. 26, 2010), available on Westlaw at 2010 COMFINNL 33.

The Seventh Circuit suggested that there is something anomalous about barring a liquidation trustee, but not the rest of the world's potential assignees, from bringing a suit like this. App., *infra*, 4a. But a trustee appointed by a bankruptcy court to represent the estate is very different from the universe of other potential assignees. He is a creature of bankruptcy law with powers limited by statute, and no assignee other than the Trustee can force the bankruptcy estate to subsidize such litigation. Indeed, if the customer claims had been assigned to Grede in his personal capacity, he (or the assignors) would have had to incur the upfront costs of litigation, just like other plaintiffs. It is Grede's unique power as Bankruptcy-Court-appointed trustee to impose those costs directly on the estate that distinguishes him from all other potential assignees.[6]

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[6] In the court of appeals, Grede argued that *Sprint Commc'ns Co.* v. *APCC Servs., Inc.*, 554 U.S. 269 (2008), limits *Caplin* and overrules *Williams*. But *Sprint* does not address the litigation authority of a bankruptcy-court-appointed trustee, holding only that an assignee's standing to sue is not barred simply because any proceeds will go to the assignors. That point of assignment law is immaterial here. Whether the proceeds go to the assignors or stay with the assignee, they will not go to the estate, an issue of bankruptcy law governed by *Caplin* and not addressed by *Sprint*.

III. THIS COURT SHOULD RESOLVE THIS IMPORTANT FEDERAL QUESTION TO PREVENT SUBSTANTIAL HARM TO THE BANKRUPTCY PROCESS.

The Seventh Circuit's ruling threatens severe adverse practical consequences for numerous bankruptcy cases pending in the federal judicial system. Unless reversed, it will generate perverse (and irresistible) incentives by allowing trustees to use the estates they are supposed to represent to finance litigation against third parties on behalf of assigning creditors. Whereas litigation costs generally act to constrain private parties from pursuing unwarranted litigation, the Seventh Circuit's ruling allows a trustee to draw freely on estate assets to pursue third-party litigation. Especially where, as here, a trustee is not only guaranteed his fees and expenses from estate assets but also has a chance to earn a substantial contingency fee if he wins, even the most dutiful of trustees would be hard-pressed to resist being overly litigious. As Judge Posner has noted, courts must "be vigilant in policing the litigation judgment exercised by trustees." *Maxwell* v. *KPMG LLP*, 520 F.3d 713, 718 (7th Cir. 2008). That is particularly true with respect to litigation launched by liquidation trustees with personal incentives to bring actions funded by the bankruptcy estate.

In the name of the Liquidation Trust, Grede has effectively set himself up as an independent plaintiffs' law firm, claiming the right to file lawsuits against third parties that will not benefit the estate (or the liquidation trust) but only select claimants. But unlike in other litigation, neither Grede nor his "clients" have to pay a dime in fees or expenses, all of which he imposes on the bankruptcy estate. If Grede

loses this lawsuit, he is still a winner because the estate will pay all his fees and expenses, as well as those of the professionals he engages to assist him. And if he wins this lawsuit, he stands to garner a hefty contingency fee as well. This is the sweetest of all possible deals, one that is unprecedented, unjustified, and open to abuse.

The ruling below invites wholesale assignments of personal claims to liquidation trustees so that claimants can foist the usual costs of litigation onto the bankruptcy estate, including on creditors with no interest in the resolution of those claims and nothing to gain from their pursuit. The Seventh Circuit said this is "no skin off *the Bank's* nose." App., *infra*, 7a. But the Bank is the very target of the assigned claims in this case, giving it an interest in ensuring that Sentinel's investors are subject to normal litigation constraints. Moreover, in other cases the Bank is bound to be among the estate creditors that could be forced to subsidize litigation from which the estate cannot benefit. There will doubtless be many such cases because post-confirmation liquidation trusts are becoming an increasingly popular tool for liquidating debtors via Chapter 11 plans. See David R. Kuney, *Liquidation Trusts and the Quagmire of Postconfirmation Jurisdiction: the Case of the Disappearing Estate*, 14 J. Bankr. L. & Prac. 6 Art. 3 (2005) (noting the "increasing use of the liquidating trusts" in confirmed bankruptcy plans); Andrew M. Thau *et al.*, *Postconfirmation Liquidation Vehicles (Including Liquidating Trusts and Postconfirmation Estates): An Overview*, 16 J. Bankr. L. & Prac. 2 Art. 4 (2007) (a liquidation trust "allows a Chapter 11 plan to be confirmed, and distributions to begin, before all of the debtor's assets have been liquidated or litigation completed, because often the most complex

and time-consuming matters are left for resolution by the [trust]").

This Court should review and reverse the decision below to prevent a misuse of the bankruptcy process for private gain at the expense of the estate as a whole—precisely what the bankruptcy laws were intended to prevent. See *Howard Delivery Serv., Inc.* v. *Zurich Am. Ins. Co.*, 547 U.S. 651, 667 (2006) (the "broad purpose" of the bankruptcy statutes "is to bring about an equitable distribution of the bankrupt's estate"). As the Court stressed in *Caplin*, if any change in the existing bright-line rule is to be made, that decision must come from Congress, which alone can address the competing policy issues. See also *Jones* v. *Harris Assocs. L.P.*, 130 S. Ct. 1418, 1430-1431 (2010) (change to longstanding "workable standard" is "a matter for Congress, not the courts").

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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APPENDIX

APPENDIX A

UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

No. 09-3121

FREDERICK J. GREDE,
as Trustee of the Sentinel Liquidation Trust,
Plaintiff-Appellant,

v.

THE BANK OF NEW YORK MELLON and THE BANK OF NEW YORK MELLON CORPORATION,
Defendants-Appellees.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.
No. 09 C 1919
James B. Zagel, *Judge*

Argued February 18, 2010.
Decided March 18, 2010.

Before EASTERBROOK, Chief Judge, and KANNE and ROVNER, Circuit Judges.

EASTERBROOK, Chief Judge.

After Sentinel Management Group, Inc., entered bankruptcy, the court appointed Frederick Grede as its trustee. A plan of reorganization under Chapter 11 of the Bankruptcy Code created a trust to hold most of Sentinel's assets (valued at more than $500 million) while its business was being wound up, its investments cashed out, and its claims paid. The plan was confirmed in December 2008. No one asked for a stay or appealed, and the plan took effect.

Grede changed hats from Chapter 11 Trustee to Trustee of the Sentinel Liquidation Trust.

Sentinel was a futures commission merchant and investment manager for commodity brokers, pension funds, and wealthy persons. Many of its customers (collectively the investors) believe that Sentinel defrauded them, and they blame not only Sentinel's managers but also The Bank of New York Mellon, which was Sentinel's clearing bank, lender, and depository for investment pools. Sentinel's claims against the Bank, including those seeking to recover payments that the Trustee characterizes as preferential transfers or fraudulent conveyances, were transferred to the Trust. Investors' claims against the Bank did not belong to Sentinel and were not part of the bankruptcy estate. But the terms of the Liquidation Trust permit investors to assign their claims to it for collection, and many of Sentinel's investors have done just that. The Trustee filed this action under the diversity jurisdiction to pursue the investors' claims.

The Bank made two threshold objections: first that the assignment was a collusive maneuver for the purpose of creating jurisdiction, which if so would knock out subject-matter jurisdiction, see 28 U.S.C. § 1359; and second that the Trustee lacks "standing" to pursue the investors' claims. We put "standing" in scare quotes because the usage is abnormal. A trustee owns the trust's assets. If these assets are depleted by fraud, the trustee may sue to redress the injury, even though the trust will distribute all of the proceeds to its beneficial owners. Indeed, a claim's assignee may sue even when the claim was assigned for the purpose of collection and there is no formal trust. See *Sprint Communications*

Co. v. APCC Services, Inc., 128 S. Ct. 2531 (2008). But in 1972 the Supreme Court used the phrase "lacks standing" to describe its conclusion that a bankruptcy trustee may not sue on behalf of investors who thought that a third party's acts had injured them and the debtor jointly. *Caplin v. Marine Midland Grace Trust Co.*, 406 U.S. 416 (1972). The Court used the language of "standing" to refer, not to injury, causation, and redressability, the three ingredients of standing, see *Steel Co. v. Citizens for a Better Environment*, 523 U.S. 83, 102-04 (1998), but to whether Congress had authorized a trustee to pursue a given kind of action. Whether a given action is within the scope of the Code is a question on the merits rather than one of justiciability. To avoid confusion, therefore, the rest of this opinion refers to the Trustee's "authority" to act on behalf of the investors, rather than his "standing" to do so.

A collusive assignment is a genuine jurisdictional problem. We treat an assignment as collusive when its sole function is to shift litigation from state to federal court. See, e.g., *Steele v. Hartford Fire Insurance Co.*, 788 F.2d 441, 444 (7th Cir. 1986); *Hartford Accident & Indemnity Co. v. Sullivan*, 846 F.2d 377, 382 (7th Cir. 1988).

Assignment to a trust could be designed to take advantage of the rule that a trust's citizenship is that of the trustee, rather than the beneficiaries, for the purpose of 28 U.S.C. § 1332(a). See *Navarro Savings Association v. Lee*, 446 U.S. 458 (1980). Cf. *Northern Trust Co. v. Bunge Corp.*, 899 F.2d 591 (7th Cir. 1990) (a non-trustee holder of injured parties' claims has the same citizenship as the claims' owners). But it would not be sensible to put the assign-

ments to the Sentinel Liquidation Trust in the collusive category.

The Bank is a citizen of New York; many investors are not, and many individual claims exceed $75,000, so those investors could sue under the diversity jurisdiction in their own names. Or one investor could sue on behalf of a class; only the plaintiff's citizenship would count, just as only a trustee's citizenship counts. See *Snyder v. Harris*, 394 U.S. 332, 340 (1969). What's more, the Trust already is suing the Bank in federal court in its capacity as holder of Sentinel's claims to recover preferential or fraudulent transfers; the investors' claims could be added under the supplemental jurisdiction. See 28 U.S.C. § 1367; *Exxon Mobil Corp. v. Allapattah Services, Inc.*, 545 U.S. 546 (2005). The assignments thus do not move litigation from state to federal court; instead they facilitate efficient aggregation of claims, just as Fed. R. Civ. P. 23 does. Subject-matter jurisdiction is secure.

The district court dismissed the suit after concluding that the Trustee lacks authority to act on behalf of the investors. 409 B.R. 467 (N.D. Ill. 2009). It relied on *Caplin* and one circuit's conclusion that *Caplin's* rule applies even after the bankruptcy ends. *Williams v. California 1st Bank*, 859 F.2d 664 (9th Cir. 1988). The Trustee observes that this approach makes him the only one of the world's 6.8 billion people who cannot sue on assignments of the investors' claims; the Bank replies that the problem is not that Grede used to be a trustee in bankruptcy, but that the Trust holds assets that came from Sentinel's estate. According to the Bank, the Trust may use its assets to subsidize suit on the assigned claims; if the Trust loses, its beneficial owners will be out of pock-

et. The Bank submits that, in order to protect the Trust's beneficial owners, the Trustee should be forbidden to champion third-party claims. At least one circuit has rejected that argument, and the *Williams* decision, in holding that a liquidating trust created in bankruptcy may accept and sue on assignments of third-party claims. *Semi-Tech Litigation, LLC v. Bankers Trust Co.*, 272 F. Supp. 2d 319, 323-24 (S.D.N.Y. 2003), affirmed & adopted, 450 F.3d 121, 123 (2d Cir. 2006). We must choose between the second circuit's holding and the ninth's.

Caplin gave three reasons for its conclusion that a bankruptcy trustee may not pursue third-party claims. First, the Bankruptcy Act of 1898 elaborately specified the powers of trustees in bankruptcy; none of its provisions so much as hinted that bankruptcy judges could transfer third-party claims to trustees. 406 U.S. at 428-29. (Six years after *Caplin*, the Bankruptcy Code of 1978 replaced the Bankruptcy Act of 1898. The parties agree that the Code does not make any change material to the issue in *Caplin*.) Second, the third-party claims in *Caplin* might have created a right of subrogation, which would have required the debtor in bankruptcy to reimburse the third-party defendant for anything the trustee collected on behalf of the investors. The Court did not see any benefit in such a roundabout process. 406 U.S. at 429-31. Third, permitting a bankruptcy trustee to pursue third-party claims creates a risk of inconsistent or double recovery-because the claims had been placed in the trustee's hands by the judge rather than by the claims' owners. 406 U.S. at 431-34. None of these reasons applies to suit by a liquidation trustee on assigned claims.

Although the terms of the Bankruptcy Code govern the permissible duties of a trustee *in* bankruptcy, the terms of the plan of reorganization (and of the trust instrument) govern the permissible duties of a trustee *after* bankruptcy. A liquidation trust is no different in this respect from a reorganized debtor. No one believes that the powers and duties of the managers at United Airlines, which emerged from bankruptcy when the court approved its plan of reorganization in 2006, depend today on the terms of the Code. They depend on the terms of the plan, on United's articles of incorporation, and on rules of corporate rather than bankruptcy law. People are tempted to assume that bankruptcy is forever and that the Code continues to regulate the conduct of former debtors. We have held otherwise. See *In re Zurn*, 290 F.3d 861 (7th Cir. 2002); *Pettibone Corp. v. Easley*, 935 F.2d 120 (7th Cir. 1991). The Sentinel Liquidation Trust is a post-bankruptcy vehicle, just like the reorganized United Airlines. (That the bankruptcy proceeding continues after the plan's approval does not affect this conclusion; proceedings after the plan is confirmed often are necessary to value particular claims and distribute proceeds, but this process is independent of the reorganized entity's current operations.)

So much for *Caplin's* first reason. The Bank does not seriously contend that a right of subrogation would enable it to make any claim against Sentinel's assets; the Bank would have had to make such an argument in the bankruptcy court, and it did not. Today the Bank's rights against the Trust are limited by the plan of reorganization. As for *Caplin's* third reason: the Trust holds only those third-party claims that investors have assigned, so there is no possibility of inconsistent dispositions or duplicative

recoveries. By proceeding on the investors' voluntary assignments rather than a bankruptcy judge's directive, Sentinel's plan of reorganization cures *Caplin's* third problem.

The Bank cites *Caplin* often but in the end does not rely on any of its three reasons. As we've mentioned, the Bank's principal argument is that the Trust should not be allowed to deplete its assets by the expense of litigating the investors' claims. If the Trust pursues these claims and loses, legal fees and other expenses are out the window, for the investors assigned their claims without promising to underwrite the Trust's litigation. Yet this is no skin off *the Bank's* nose. The Bank is not among the Trust's beneficial owners-and, if it were, the time to object would have been when the plan of reorganization was proposed. The possibility that the Trust would use some of its assets to sue on behalf of the assignors was apparent to any reader of the plan or the trust documents. Any beneficial owner could have objected and demanded that the assignors contribute not only their claims but also liquid assets. No one objected on this ground, however, and the plan, having taken effect, is not open to the sort of collateral attack that the Bank now wages. *In re UNR Industries, Inc.*, 20 F.3d 766 (7th Cir. 1994); *In re Harvey*, 213 F.3d 318, 321 (7th Cir. 2000).

The Bank is trying to fend off the Trust's claims not by standing on its own rights, but by asserting that the litigation might injure strangers (the Trust's beneficiaries). It is a basic principle that litigants can't invoke the rights of third parties. American law recognizes a few instances in which *jus tertii* claims ("third-party standing") are allowed, but these are rare. See *Kowalski v. Tesmer*, 543 U.S. 125 (2004)

(discussing authority); cf. *MainStreet Organization of Realtors v. Calumet City*, 505 F.3d 742 (7th Cir. 2007) (discussing prudential limits when third parties suffer the principal injury). The Bank does not even try to show that it meets the requirements for third-party standing, let alone for the sort of third-party claim that would justify a belated challenge to a confirmed plan of reorganization.

Although the Bank tries to recast this argument as one about Delaware trust law (the Trust is a business trust under Delaware law), this line of argument does more to show *Caplin's* irrelevance than to escape from the problem that the Bank is asserting strangers' supposed entitlements. For if the Trust's ability to accept and sue on the assigned claims really does depend on Delaware law, then *Caplin*, which rests on federal bankruptcy law, does not have a role to play. We need not get into this subject, however, because the Trust's beneficial owners, rather than the Bank, are the right persons to make any contention that the Trust should not have accepted the assignments of the investors' choses in action.

We conclude that *Caplin* does not apply to the activities of a liquidating trust created by a plan of reorganization (or, for that matter, an ex-debtor operating under a confirmed plan). The judgment of the district court is reversed, and the case is remanded for further proceedings consistent with this opinion.

APPENDIX B

UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION

FREDERICK J. GREDE, not individually but as Liquidation Trustee of the Sentinel Liquidation Trust, Assignee of certain claims,

Plaintiff,

v.

THE BANK OF NEW YORK MELLON and THE BANK OF NEW YORK MELLON CORP.,

Defendants.

No. 09 C 1919.

July 28, 2009.

MEMORANDUM OPINION AND ORDER

JAMES B. ZAGEL, District Judge.

I. BACKGROUND

Plaintiff, Liquidation Trustee as Assignee of certain creditor claims, brings this action against Defendants alleging that they aided and abetted debtor investment manager's breach of fiduciary duty to its customers, aided and abetted debtor's fraud, and acted negligently toward debtor's customers. Defendants now move to dismiss the complaint for lack of standing, pursuant to Federal Rule of Civil Procedure 12(b)(1), and for failure to state a claim under Rule 12(b)(6). For the following reasons, Defendants' motion is granted.

II. STATEMENT OF RELEVANT FACTS

Plaintiff in this case is the Liquidation Trustee of the Sentinel Liquidation Trust. Sentinel was an investment manager for sophisticated clients, including commodity brokers, hedge and pension funds, and financial institutions. Sentinel was a Bank of New York ("BNY") customer, initially as a client of its custodial services group and then as a client of its clearing services division. Trustee alleges that Sentinel insiders engaged in a fraudulent scheme to leverage customer assets, putting the company and the customers at risk if the market were to decline. This is exactly what happened, and in August 2007, Sentinel collapsed and filed for bankruptcy. Trustee alleges that Defendants knew of and participated in this scheme by establishing an account structure that facilitated the commingling of assets that should have been segregated and the misuse of customer funds. In early 2008, Trustee filed an adversary action against Defendants on the basis of their alleged misconduct, seeking to recover for the Liquidation Trust the value of the customer assets that he alleges were improperly desegrated and used as leverage. See *Grede v. Bank of New York*, No. 08 C 2582, 2009 WL 188460 (N.D. Ill. 2009). In 2009, Trustee filed another action against Defendants, this time as assignee of certain of Sentinel's customers' claims, seeking to recover the millions lost by these customers. Because Plaintiff's allegations in this case (the "customer action") are substantially similar to those asserted in the initial action against Defendants (the "Trustee action"), I see no need to restate them in great detail and refer the reader to the Trustee action for a more comprehensive factual background with regard to debtor Sentinel's business and the al-

leged misconduct by Defendants. *Id.* I will, however, address a few facts relevant to this case specifically.

On December 15, 2008, the bankruptcy court entered an order confirming the Fourth Amended Chapter 11 Plan of Liquidation for Sentinel (the "Plan"). Trustee, formerly the Chapter 11 trustee for Sentinel, became the Liquidation Trustee for the Sentinel Liquidation Trust (the "Trust"), which represents Sentinel's estate. As part of the Plan, claims held by Sentinel's customers who accepted the Plan were transferred to the Liquidation Trust, and the Trust became the assignee of the claims. The Plan established a distinct tranche of the Trust to hold the non-estate customer claims assigned to the Trust. Claims held in this tranche do not become property of the estate, and non-assignors of claims are entitled to no distributions from this special tranche. It is the assigned customer claims that Trustee now asserts against Defendants.[1] Defendants move to dismiss Trustee's complaint for lack of standing, pursuant to Federal Rule of Civil Procedure 12(b)(1), and for failure to state a claim under Rule 12(b)(6). Because Trustee does not have standing to bring the assigned claims, I need not reach the issue of the sufficiency of the complaint.

III. DISCUSSION

A. Whether Defendants' Standing Challenge is Barred by Res Judicata

The first issue I must address is Trustee's contention that res judicata bars BNY's standing chal-

[1] Trustee asserts the claims of customers who accepted the Plan together with those of certain additional customers who did not accept the Plan.

lenge. Because the assignments at issue were made pursuant to Sentinel's chapter 11 liquidation plan-a plan approved by the bankruptcy court-Trustee maintains that Defendants are now launching "a collateral attack on the power of the Bankruptcy Court to effect an assignment of the claims by approving the Plan." *Semi-Tech Litig., LLC v. Bankers Trust Co.*, 272 F. Supp. 2d 319, 324 (S.D.N.Y. 2003). I am not persuaded by this argument and find that res judicata does not bar BNY's standing challenge.

"To apply res judicata, three essential elements must exist: (1) a final judgment on the merits in an earlier action; (2) an identity of the cause of action in both the earlier and later suit; and (3) an identity of parties or privies in the two suits." *Wade v. Hopper* 993 F.2d 1246, 1252 (7th Cir. 1993). "The doctrine of res judicata bars suit on matters which were raised or could have been raised in previous litigation between the parties." *Matter of Vitreous Steel Products Co.*, 911 F.2d 1223, 1234 (7th Cir. 1990). According to Trustee, Defendants have litigated their objections to the confirmation of the Plan. Although they did not challenge Trustee's standing to bring the assigned claims, they did challenge the assignments on other grounds. It was during that proceeding, Trustee argues, that the standing challenge should have been made.

This argument is problematic for two reasons. First, it appears that Defendants' objections to the plan were never ruled on, since the parties settled their dispute with regard to the Plan. Next, Trustee's contention that Defendants essentially waived their standing objection is unavailing. Standing, a jurisdictional question, cannot be waived. *Wiggins v. Martin*, 150 F.3d 671, 673 (7th Cir. 1998). While "[i]t is a

well-established principle of bankruptcy law that a party with adequate notice of a bankruptcy proceeding cannot ordinarily attack a confirmed plan," *In re Harvey*, 213 F.3d 318, 321 (7th Cir. 2000) (citing 11 U.S.C. § 1327(a)), confirmation of a bankruptcy plan "is res judicata only as to issues that can be raised in the less formal procedure for contested matters[.]" *Strong v. IRS* (*In re Strong*), 203 B.R. 105, 114 (Bankr. N.D. Ill. 1996) (holding that "confirmation generally cannot have preclusive effect as to the validity of a lien, which must be resolved in an adversary proceeding as mandated by Fed. R. Bankr. P. 7001(2)."). "[A] confirmed plan acts more or less like a court-approved contract or consent decree that binds both the debtor and all the creditors." *In re Harvey*, 213 F.3d 318, 321 (7th Cir. 2000). But proceedings to recover money are adversarial under the Federal Rule of Bankruptcy Procedure 7001(1) and are more formal than contested matters. *In re Matter of Beard*, 112 B.R. 951, 955 (Bankr. N.D. Ind. 1990). Adversarial matters are initiated by a summons and complaint, to which defendants are expected to respond. *Id.* Contested matters are typically dealt with by motion and a response is generally not necessary. *Id.* "If an adversary proceeding is required to resolve the disputed rights of third parties, the potential defendant has the right to expect that the proper procedures will be followed." *Id.* It is difficult to see how the issue of standing in this adversarial action could have been litigated as part of the less-formal confirmation process before the adversarial action itself was even filed.

In support of his argument, Trustee relies on *Semi-Tech*, where the plaintiff, an entity created by a

liquidation plan, brought claims assigned by debtor's creditors against a third-party defendant.[2] The defendant challenged the plaintiff's standing generally to assert such claims and also challenged the validity of the Bankruptcy Court's assignment of the claims. The court found that the attack on the validity of the assignments was a collateral one on the power of the bankruptcy court, barred by res judicata, but addressed the general standing challenge on the merits. In this case, Defendants are not claiming that assignments pursuant to the liquidation plan are invalid, only that Trustee has no standing to bring the assigned claims. Similar to *Semi-Tech*, the standing issue before me must be addressed on the merits.

B. Standing

Defendants argue that the Trustee lacks standing to bring this suit because the individual claims at issue here belong to third-party creditors and are non-estate claims. Federal bankruptcy law "places a trustee in the shoes of the bankrupt corporation and affords the trustee standing to assert any claims that

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[2] Trustee also relies on *In re J. Allan Steel Company*, 323 B.R. 425, 433 (Bankr. W.D. Pa. 2005) for the proposition that Defendants should have raised their standing challenge during the confirmation stage. In that case, the court held that the defendant's standing challenge to creditors' committee's adversarial action, authorized by the Bankruptcy Court, was barred by res judicata because the defendant "had ample opportunity at the confirmation hearing to object to the provision of debtor's plan delegating the power to bring avoidance actions to the Committee[,]" but failed to do so. *Id.* However, the court points to no case law in support of its conclusion that the issue of standing in a future adversarial proceeding should be decided at the time of a bankruptcy plan's confirmation hearing. I respectfully decline to follow the court's reasoning in that case.

the corporation could have instituted prior to filing its petition for bankruptcy." *In re CBI Holding Co., Inc.*, 529 F.3d 432, 454 (2d Cir. 2008). The claims presented here are, according to the Amended Complaint, "the direct claims of certain of Sentinel's customers." In other words, Sentinel's customers are seeking recovery for harms BNY allegedly caused them, not Sentinel itself. Defendants maintain that because these claims involve monies owed not to the estate, but to the customers directly, the Trustee has no authority, and thus no standing, to bring this suit on their behalf.

Trustee makes essentially two arguments in support of his contention that he does indeed have standing to bring the assigned customer claims. First, according to Trustee, the fact that the claims at issue were assigned to the Liquidation Trust under the Plan approved by the bankruptcy court makes all the difference. He argues that as assignee, he is stepping directly into the shoes of the assignors and should not be treated any differently from any other assignee. Second, Trustee argues that where any recovery would not go directly to particular assignors but would be shared by them pro rata, the Trustee is the real party in interest, and should not be barred from bringing the assigned actions.

"[A] litigant seeking relief in federal court must satisfy both constitutional and prudential limitations in order to have standing to sue." *Locals 666 and 780 of Intern. Alliance of Theatrical Stage Employees and Moving Picture Mach. Operators of United States and Canada, AFL-CIO v. U.S. Dept. of Labor*, 760 F.2d 141, 143 (7th Cir. 1985). "The prudential limitations on standing are those imposed by the courts themselves[.]" *Id.* "One well-established prudential-

standing limitation is the principle that a litigant cannot sue in federal court to enforce the rights of third parties." *Rawoof v. Texor Petroleum Co., Inc.*, 521 F.3d 750, 757 (7th Cir. 2008). "When a third party has injured not the bankrupt corporation itself but a creditor of that corporation, the trustee in bankruptcy cannot bring suit against the third party. He has no interest in the suit." *Steinberg v. Buczynski*, 40 F.3d 890, 893 (7th Cir. 1994).

The liquidation trustee is specifically authorized to "collect and reduce to money the property of the estate for which such trustee serves, and close such estate as expeditiously as is compatible with the best interests of parties in interest." 11 U.S.C. § 704(1). "Property of the estate" under § 541(a) has "uniformly been interpreted to include causes of action." *Polis v. Getaways, Inc. (In re Polis)*, 217 F.3d 899, 901 (7th Cir. 2000). The United States Bankruptcy Code (the "Code"), from where a trustee derives his powers, does not authorize a trustee to "collect money not owed to the estate." *Caplin v. Marine Midland Grace Trust Co. of New York*, 406 U.S. 416, 428 (1972). In *Caplin*, the Court held that a Chapter X Trustee did not have standing to bring, on behalf of debtor's debenture holders, claims against a third party. The Court's decision was informed by three factors: (1) the Code does not authorize a trustee "to collect money not owed to the estate"; (2) it was unclear whether, where debtor and third party may have been *in pari delicto*, the third party would be entitled to be subrogated to the claims of the debenture holders; and (3) the possibility that the trustee's action would produce outcome inconsistent with any independent actions the debenture holders might themselves bring. *Id.* at 427-435. Because granting the trustee standing would have increased litigation "or

at least complicated" it, the Court declined to do so. *Id.* at 434.

Trustee first argues that this case is distinguishable from *Caplin* since the claims at issue in this case were assigned to the liquidation Trust under the Plan approved by the Bankruptcy Court. He argues that as assignee, he is stepping directly into the shoes of the assignors, and that his statutory authority is not implicated. Trustee relies on *Sprint Communications Company v. APCC Services, Inc.*, a case that did not involve a bankruptcy trustee, where the Supreme Court recognized that "an assignee can sue based on his assignor's injuries," and "federal courts routinely entertain suits which will result in relief for parties that are not themselves directly bringing suit." 128 S. Ct. 2531, 2542, 2543 (2008). Under *Sprint*, he argues, the fact that only those customers who assigned their claims will benefit from any recovery in this case is no reason to deny standing. 128 S. Ct. at 2543 (reasoning "[w]hat does it matter what the [assignors] do with the money afterward? The injuries would be redressed whether the [assignors] remit the litigation proceeds to the [customers], donate them to charity, or use them to build new corporate headquarters."). According to Trustee, he should not be treated any differently from any other assignee.

This argument is unpersuasive in light of case law involving powers of trustees. In *Williams v. California 1st Bank*, 859 F.2d 664, 666 (9th Cir. 1988),[3]

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[3] Trustee relies on *Semi-Tech Litigation, LLC v. Bankers Trust Company*, where the court found *Williams* unpersuasive and saw "no basis for treating an assignee created by, or assignments made pursuant to, a Chapter 11 plan any differently"

the Court held that the same concerns that militated against standing in *Caplin* bar a liquidation trustee from suing third parties on behalf of estate creditors even where the creditor claims are assigned to the trustee. The Court in *Williams* addressed the Trustee's authority to bring assigned creditor claims. There, the creditor-assignors were to receive the bulk of any recovery, with only administrative costs from a favorable judgment going to the estate. The Court determined that the creditors, not the estate, were the "real party in interest." *Williams*, 859 F.2d at 666. Because the trustee in that case was "attempting to collect money not owed to the estate[,]" he did not have the authority under the Code to bring the creditor claims, notwithstanding the assignment. *Id.* at 666-67. In discussing the benefits of court-approved assignment of creditor claims, the Court in *In re CBI Holding* remarked that "[a]llowing a deb-

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from an assignee or assignment created outside the bankruptcy context. 272 F. Supp. 2d 319, 324 (S.D.N.Y. 2003). In that case, the court considered neither the priority of claims nor the issue of subrogation, discussed *infra* — issues significant to this case. For this reason I am not persuaded by the court's analysis in *Semi-Tech*, and rely instead on the reasoning in *Williams*. Furthermore, in *Semi-Tech*, the court did not discuss how any recovery would be distributed, another significant matter here. In *In re CBI Holding Co., Inc.*, 529 F.3d at 459, the Second Circuit discussed *Semi-Tech's* holding "that a trustee may assert claims assigned to it by a bankrupt's creditors *for the benefit of the estate*, because those claims *can become property of the estate* under § 541(a)(7)." This suggests that the trustee must continue to act pursuant to his authority under the Code, even where he is the assignee of creditors' claims. However, in this case, the Plan explicitly states that the assigned non-estate claims shall not become property of the estate. In this way, the case before me is distinguishable from *Semi-Tech*, and the notion articulated therein that trustee assignees should not be treated any differently from non-trustee assignees does not apply here.

tor's creditors to assign their claims *for the benefit of the debtor's estate* permits debtors, creditors, and bankruptcy courts the flexibility in reorganizing or liquidating a debtor's assets necessary to achieve efficient administration of the reorganization or liquidation." 529 F.3d at 549 (emphasis added); *see also Logan v. JKV Real Estate Servs. (In re Bogdan)*, 414 F.3d 507, 512-513 (4th Cir. 2005) (holding that trustee may bring assigned creditor claims where estate is the real party in interest). Even where a trustee brings assigned claims, he is still subject to the Code's requirement that he act for the benefit of the estate.

Policy also suggests that Trustee should be treated differently from a non-trustee assignee. "As a creature of statute, the trustee in bankruptcy has only those powers conferred upon him by the Bankruptcy Code." *In re Cannon*, 277 F.3d 838, 853 (6th Cir. 2002) (citation omitted). Trustee in this case brings the assigned claims as Trustee, not in his personal capacity. As Trustee, the estate pays his legal fees and costs. Failure to prevail on his claim would diminish the assets available to creditors of the estate. It is for this reason Trustee should be limited to his powers under the Code. Trustee should not be permitted to bring claims for the benefit of the few at the expense of the many.[4]

Trustee next argues that *Williams* does not apply here since the proceeds of the assigned claims will be distributed in accordance with a court-approved

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[4] It is true that Trustee has also filed a claim against BNY on behalf of the estate, however, discovery would not be entirely duplicative and would in this action be the source of extra expense.

bankruptcy plan. In support of this position, Trustee cites *In re CBI Holding Company, Inc.*, 529 F.3d at 458, where the Court recognized a trustee's ability to bring assigned creditor actions against third parties. "We can think of many arguments against allowing a trustee to usurp the claims of a bankrupt's non-cooperating creditors that do not counsel against permitting creditors to voluntarily transfer their claims to a trustee as part of a court-approved plan of reorganization or liquidation." *Id.*[5] According to Trustee, where any recovery would not go directly to particular assignors but would be shared by them pro rata, the Trustee is the real party in interest, and *Williams* does not apply.

Trustee's analysis misses the mark. In order for the estate to be the real party in interest, any recovery must come into the estate to then be distributed according to the order of priority prescribed by the Code. In *In re Bogdan*, the court expressly distinguished the case before it from *Williams*, explaining that

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[5] The language in *In re CBI Holding* is not difficult to construe. What does it mean to say "We can think of many arguments against [usurping] that do not counsel [against assignment]"? One thing that is not said is that "all arguments against usurping do not counsel against assignment." This excerpt from *CBI* is in the language of dicta, not of holding. And it is the language of dicta because the panel understood the key issue was whether the "adverse interest" exception (allowing a trustee to step out of the "shoes" of the failed company) applied in light of the facts found by the Bankruptcy Judge. Besides the fact the language is dicta, it is not intended to be read as a thorough analysis of the proposition it mentions. It is, I noted, incomplete as a statement that trustees can sue as assignees of individual creditors. Dicta can be persuasive but the court did not intend to persuade, or it would have said more.

> Unlike the investors in *Williams*, the [assignors] in this case will recover, if at all, by sharing from the general assets of the estate on a pro rata basis *with all other creditors*. So, unlike the trustee in *Williams*, Bogdan's trustee is seeking to collect money it claims the alleged coconspirators owe the trustee as assignee and *representative of the estate*, not money owed to specific creditors. Accordingly, Bogdan's estate is the real party in interest in this adversary proceeding.

In re Bogdan, 414 F.3d at 513 (emphasis added). In *Bogdan*, the fact that any recovery would go to the estate, from which the assignors, like all other creditors, would recover on a pro rata basis, meant that the trustee was bringing action to collect money owed to the estate for the benefit of all of the creditors. The court in *Steinberg v. Kendig (In re Ben Franklin Retail Stores, Inc.)*, 225 B.R. 646, 651 (Bankr. N.D. Ill. 1998) drew a similar distinction, noting that there, "the estates are the real parties in interest, and any proceeds will come into the estates, to be distributed in accordance with the bankruptcy code."

In this case, under the Plan, recovery on the assigned claims would be pooled together into a special tranche of the Trust and "distributed to the assignors in accordance with the priorities established by the Plan." It is true that the tranche is part of the Trust, however non-assignors may not recover from the tranche. This structure excludes a significant intermediary link in the chain of recovery-that the proceeds come "into the estate," to be distributed pro rata among assignors and non-assignors alike. Without this link, the estate has no interest in the claims,

and Trustee has no authority under the Code to bring them. One goal of the Bankruptcy Code is to ensure equal distribution among creditors, allowing for preferential treatment of certain creditors pursuant only to congressional authorization. *Howard Delivery Service, Inc. v. Zurich American Ins. Co.*, 547 U.S. 651, 655 (2006) (citations omitted). Under 11 U.S.C. § 725, priority and secured claims are to be paid before any distributions are made to unsecured creditors. If any funds remain after priority claims are paid, then unsecured creditors may receive a distribution. *Monarch Air Service v. Solow (In re Midway Airlines, Inc.)*, 383 F.3d 663, 669 (7th Cir. 2004). In this case, Sentinel customers are unsecured creditors. So although under the recovery structure put forth here, the assignors must divide any proceeds pro rata among themselves, they are essentially circumventing the order of priority of claims established by the Code. For this reason, it is crucial that the estate be the real party in interest, and that the Trustee not be allowed to do by virtue of assignment what he may not do on his own.

Further militating against Trustee's standing here is the possibility of subrogation. In *Williams* the court addressed the issue of whether, where the debtor and Defendant are *in pari delicto*, Defendant would be able to subrogate itself to the assignors' position and recoup any recovery to which assignors may be entitled. 859 F.2d at 667. The Court held that where such a possibility exists, there would be little advantage in giving trustee standing to sue. *Id.* at 667 (citing *Caplin*, 406 U.S. at 430). While the defense of *in pari delicto* has been raised by BNY against the Trustee, the issue has not yet been decided, neither has the validity of BNY's lien upon Sentinel's assets. But, as the Supreme Court noted in

Caplin, regardless of whether subrogation is appropriate here,

> the fact remains that in every reorganization there is going to be a question of how much the trustee in reorganization should be permitted to recover on behalf of the debenture holders. The answer is, of course, whatever he cannot recoup from the corporation.... In other words, debenture holders will not be able to recover damages from the indenture trustee until the reorganization is far enough along so that a reasonable approximation can be made as to the extent of their losses, if any.

406 U.S. at 430-431. The Court reasoned that the creditors should therefore represent their own interests and decide for themselves whether or not it would be "worthwhile" to seek recovery on any losses. It is true that the assignments in this case reflect the creditors' decision as to whether to proceed with their claims, but the Court's point is well taken — we do not know at this time what the customers' damages, unsatisfied by the bankruptcy proceeding, will be. Moreover, with subrogation as a possibility, "it is as difficult here as it was in *Caplin* to see what advantage there is in giving the trustee standing to sue." *Williams*, 859 F.2d at 667.

Trustee maintains that, "[t]aken to its logical extension, BNY's argument would mean that the customers could have validly assigned their claims to anyone in the world except the liquidation trust." However, were the customers to assign their claims to someone else, or to pursue them on their own, the same considerations with regard to order of priority and subrogation would be implicated. In *Shatkin v.*

Bank of New York Mellon Corporation, 2008 WL 2446837, No. 07 Civ. 7928(PAC), at *2 (S.D.N.Y. June 17, 2008), one of the assignor/creditors involved in this action filed a putative class action against Defendants alleging the same misconduct asserted in the Trustee action against BNY. In its opinion staying the proceeding pending the outcome of the proceeding in Bankruptcy Court, the court in *Shatkin* noted that

> Plaintiff, putative class members, and BNY are parties to the bankruptcy proceeding; the Bankruptcy Court will determine whether BNY had a valid, first-priority security interest in and lien upon the assets at issue and how the remainder of Sentinel's assets are to be distributed; and, as a consequence of this proceeding, Plaintiff and the putative class members may be compensated for any injuries allegedly sustained.

Id. The reasons for the stay reflect several of the same concerns that informed the Court's decision in *Caplin*. While Trustee is correct that the customers could assign their claims to someone other than Trustee without being barred from pursuing the claims, that is not to say that the claims brought by another assignee would go forward uninhibited. The prudential limitations on a trustee's standing imposed in *Caplin* with regard to Trustee's standing apply here, notwithstanding the assignment of claims.[6] Indeed, if the Trustee could bring these

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[6] The court in *Caplin* pointed to the potential of inconsistent actions by the creditors on their own behalf as another reason to deny the trustee standing. Trustee argues that "It makes no sense to reject standing to one plaintiff because some other per-

claims, there would be good reason to stay proceedings on those claims as Judge Crotty stayed Shatkin's claims.

IV. CONCLUSION

For the foregoing reasons, Defendants' motion to dismiss is granted.

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son might have a claim against the same defendant." However, the Court was concerned with the inconsistency of the trustee's suits on behalf of a certain creditor with any independent action that same creditor would himself bring. 406 U.S. at 432. Judge Crotty's stay of the proceeding in *Shatkin* suggests some regard for such possible inconsistency, where Shatkin, a party to the bankruptcy proceeding and an assignor in this case, brought his own claim in a separate proceeding. It is not difficult to imagine the possibility of inconsistency with regard to these claims.

APPENDIX C

UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

No. 09-3121

FREDERICK J. GREDE,
as Trustee of the Sentinel Liquidation Trust,
Plaintiff-Appellant,

v.

THE BANK OF NEW YORK MELLON and THE BANK OF NEW YORK MELLON CORPORATION,
Defendants-Appellees.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.
No. 09 C 1919
James B. Zagel, *Judge*

April 16, 2010

Before
FRANK H. EASTERBROOK, *Chief Judge*
MICHAEL S. KANNE, *Circuit Judge*
ILANA DIAMOND ROVNER, *Circuit Judge*

Order

Defendants-appellees filed a petition for rehearing and rehearing en banc on April 1, 2010. No judge in regular active service has requested a vote on the

petition for rehearing en banc,* and all of the judges on the panel have voted to deny rehearing. The petition for rehearing is therefore DENIED.

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* Judge Flaum did not participate in the consideration of this petition.

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No. 10-232

Supreme Court, U.S.
FILED
SEP 17 2010
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IN THE
Supreme Court of the United States

THE BANK OF NEW YORK MELLON AND
THE BANK OF NEW YORK MELLON CORPORATION,
Petitioners,

v.

FREDERICK J. GREDE, AS TRUSTEE OF THE
SENTINEL LIQUIDATION TRUST,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

RESPONDENT'S BRIEF IN OPPOSITION

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QUESTION PRESENTED

In *Sprint Communications Co. v. APCC Services, Inc.*, 554 U.S. 269, 128 S. Ct. 2531 (2008), the Supreme Court held that an assignee of a claim for collection purposes is the real party in interest and therefore has standing to pursue the assigned claim even if the assignee is obligated to pay all of the recoveries received on account of the assigned claim to the assignor. Applying *Sprint*, the Seventh Circuit concluded that the Sentinel Liquidation Trust (the "Trust"), an entity formed under Delaware law to implement a confirmed chapter 11 plan, had the authority to pursue claims creditors had assigned to the Trust against The Bank of New York Mellon and The Bank of New York Mellon Corporation (the "Bank" or "Petitioner"). In so holding, the Seventh Circuit rejected the Bank's argument that the Trust was improperly using general Trust assets for the benefit of only a select group of its beneficiaries. It concluded that the Bank had no basis to complain about a perceived injury to the Trust's beneficiaries. Furthermore, the Bank, which was a creditor of the chapter 11 debtor and an active participant in its chapter 11 case, did not object to the assignment of creditor claims against it to the Trust before the Bankruptcy Court confirmed the plan of reorganization that created the Trust. The Seventh Circuit held that by failing to object at that time, the Bank missed its opportunity to complain about the formation and powers of the Trust. The question presented is:

Whether a defendant in a lawsuit brought by a post-confirmation state law trust created to implement a plan of reorganization can collaterally attack the trust's authority post-bankruptcy to pursue claims against it on the basis of injuries it claims the trust's beneficiaries may suffer if the claims against it proceed.

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RESPONDENT'S BRIEF IN OPPOSITION

This Court should decline to review the Seventh Circuit's decision because it does not conflict with this Court's precedent or the Bankruptcy Code, involve a true Circuit split or threaten substantial harm to the bankruptcy process. The Seventh Circuit's decision merely rejects the Bank's overreaching efforts to avoid answering charges of its own misconduct by raising concerns that affect only third parties' interests (which concerns those third parties are not raising themselves). In so ruling the Seventh Circuit relies squarely and correctly on *Sprint Communications Co., L.P. v. APCC Services, Inc.*, 554 U.S. 269, 128 S. Ct. 2531 (2008), and reaches the same result this Court reached in *United Student Aid Funds, Inc. v. Espinosa*, -- U.S. --, 130 S. Ct. 1367 (2010).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Bank asserts that two statutory provisions are involved in this case: 11 U.S.C. §§ 323(a) and 704(a)(1). Neither of these provisions, however, in fact applies as both only govern the conduct of trustees operating during a bankruptcy case. The Trust in this case was formed post-confirmation and Frederick J. Grede, its trustee, is not now, and was not at the time the lawsuit in question was filed, a bankruptcy trustee. Further, section 704(a)(1) could not apply in any event because the underlying bankruptcy case was a case under chapter 11 of title 11, and not a chapter 7 case. 11 U.S.C. § 103(b)

states: "[s]ubchapters I and II of chapter 7 of this title apply only in a case under such chapter." Section 704(a)(1) is found in subchapter I of chapter 7. Further 11 U.S.C. § 1106(a) excludes section 704(a)(1) from the list of section 704 duties that apply to chapter 11 trustees.

STATEMENT OF THE CASE

a. Sentinel's Business, Its Misuse Of Customer Funds, And The Bank's Participation.

Sentinel Management Group, Inc. ("Sentinel"), the debtor in the underlying bankruptcy case, was registered as a futures commission merchant and investment advisor. (C.A. App. 10 at ¶ 17.) The Bank acted as Sentinel's clearing bank, its lender and its depository institution. (C.A. App. 13-15 at ¶¶ 35, 37-39.) Beginning in 2003, without informing its customers, Sentinel changed the nature of its investments and began using significant leverage, which put its customers' assets at risk if the market moved adversely. (C.A. App. 19 at ¶ 56.) Although the Bank had entered into agreements acknowledging that the assets in Sentinel's accounts were customer funds that would never be subject to the bank's lien or applied to offset any indebtedness of a third party (C.A. App. 13-14 at ¶¶ 32, 35, 37), it nonetheless established a securities clearing system that required Sentinel to funnel all its purchases and sales of securities through accounts against which the Bank held a security interest. The Bank put the securities into these liened accounts without regard to whether the securities were purchased for Sentinel (and thus fair game for the Bank's liens) or

for its customers (and not available to secure the Bank's debt). (C.A. App. 14-15 at ¶ 38.)

Senior officers of the Bank knew that Sentinel was using its loan to finance a leveraged investment strategy. (C.A. App. 23-26 at ¶¶ 70-72, 78.) The Bank also knew that Sentinel was representing in financial reports submitted to regulators that it had no bank loans whatsoever, and that all of its customer securities were properly held in segregated accounts. (C.A. App. 22, 29, 30 at ¶¶ 69, 97, 101.) In addition, senior officers of the Bank knew that Sentinel had minimal capital of its own (less than $2 million), and that the collateral supporting the loan to Sentinel consisted of assets Sentinel had no right to pledge. (C.A. App. 31-33, 39 at ¶¶ 102-104, 110, 130-131.) When Sentinel collapsed, the Bank asserted a lien over hundreds of millions of dollars in securities that it should have been holding in segregated customer accounts. (C.A. App. 7 at ¶¶ 3-4.)

b. Sentinel's Bankruptcy Filing.

On August 17, 2007, Sentinel filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code. (C.A. App. 352.) On August 29, 2007, the Bankruptcy Court approved the United States Trustee's appointment of Mr. Grede to serve as Sentinel's chapter 11 trustee. (*Id.*)

c. The Plan, The Bank's Objections, And The Confirmation Process.

On May 12, 2008, the chapter 11 trustee and the statutory committee appointed to represent Sentinel's creditors jointly proposed a plan of

liquidation (the "Plan"). (C.A. App. 346.) To facilitate recoveries against the Bank and other third parties allegedly involved in the fraud that led to Sentinel's bankruptcy, the Plan provided for the creation of a Trust that would pursue litigation assets. (C.A. App. 86-95 at ¶¶ 6.1-6.21.) The Plan also provided that the Trust would receive, among other things, the estate's causes of action against third parties. (C.A. App. 91 at ¶ 6.12.)

In addition, the Plan gave Sentinel's unsecured customer creditors the option when voting on the Plan to elect to assign Sentinel-related causes of action against the Bank and others to the Trust, for prosecution by the Trust at the discretion of the Trust's trustee (the "Liquidation Trustee"). (*Id.*) In return, the assignors generally would be paid the money recovered from the assigned claims on a *pro rata* basis. (C.A. App. 85 at ¶ 4.5(a), 91 at ¶ 6.12.)

After the Plan was filed, the Bank objected to the Plan and participated extensively in the two-day confirmation hearing. (C.A. App. 190-227, 229-244, 256, 276-284, 286, 311-313, 321-327.) The Bank objected to the treatment of its disputed secured claim and alleged that the Plan was not proposed in good faith because it allegedly would be implemented outside of the control of the Bankruptcy Court. (C.A. App. 226-227.) The Bank did not object to the assignment of creditor claims against it to the Trust, or argue that post-confirmation the Liquidation Trustee would lack standing to prosecute the assigned claims. (C.A. App. 191-192, 229-244.)

Although the Bank ultimately withdrew its objections to the Plan before the Bankruptcy Court

ruled (C.A. App. 245-252, 253-254), the Bankruptcy Court was still obligated to determine independently that the Plan complied with 11 U.S.C. § 1129. (C.A. App. 355-56.) On December 15, 2008, the Bankruptcy Court issued a 67-page Memorandum Opinion setting forth its reasons for confirming the Plan and entered a Confirmation Order. (C.A. App. 346-412.) Neither the Bank nor any of the other objectors appealed the Confirmation Order. The Confirmation Order is now a final order.

d. Implementation Of The Plan.

On December 17, 2008, Sentinel's Plan became effective and the Trust was created. (C.A. App. 117.) On that date, Mr. Grede resigned as the chapter 11 trustee and accepted the appointment as Liquidation Trustee, the Sentinel bankruptcy estate transferred its assets to the Trust, and creditors that had agreed to assign their causes of action to the Trust did so. (C.A. App. 87 at ¶ 6.3, 88 at ¶ 6.4.) The Plan and Trust Agreement gave the Liquidation Trustee discretion to prosecute or settle all of the Trust's causes of action, including those assigned to the Trust by creditors as he deemed appropriate, in general subject only to the oversight of the Liquidation Trust Committee. (C.A. App. 87-89 at ¶¶ 6.3, 6.5, 120-123 at ¶¶ 2.2, 2.5.)

e. Actions Against the Bank.

While he was still serving as chapter 11 trustee, Mr. Grede filed a lawsuit against the Bank asserting claims that belonged to the bankruptcy estate. In that case, which is still pending in District Court, he sued the Bank in his capacity as the chapter 11 trustee, *inter alia*, to recover preferential and

fraudulent transfers, for equitable subordination of the Bank's secured claim, and for aiding and abetting the Sentinel insiders' breach of their fiduciary duties to Sentinel. The District Court dismissed the aiding and abetting claim, ruling that the *in pari delicto* doctrine barred the claim, but allowed the balance of the case to proceed. *See Grede v. Bank of New York*, No. 08-C-2852, 2009 WL 188460, at *9 (N.D. Ill. Jan. 27, 2009). The District Court recently tried that case and has it under advisement now.

After the Plan became effective and the Trust was created, the Liquidation Trustee brought a second case against the Bank asserting the claims that Sentinel's creditors had assigned to the Trust and to which the *in pari delicto* defense does not apply. (C.A. App. 6-53.) The Bank moved to dismiss this action under Rule 12(b)(1) and (6), arguing that the Liquidation Trustee lacked standing to bring the assigned claims and alternatively failed to state valid causes of action. (Pet. App. 9a.) This second lawsuit is the action at issue in this appeal.

f. The Decisions Below.

The District Court granted the Bank's motion to dismiss. The District Court allowed the Bank to raise what were new and collateral objections to the final Confirmation Order approving the Plan because the Bank had voluntarily withdrawn different objections to the Plan before the Confirmation Order was entered. The District Court concluded that this was acceptable because the Bank's original (and different) objections "were never ruled on." (Pet. App. 12a-13a.) The District Court also held that the

question of the Trust's authority to prosecute the claims assigned to it was jurisdictional so the Bank could raise the issue belatedly. (*Id.*) The District Court then reasoned that allowing the Liquidation Trustee to bring suit on the assigned claims would be outside the scope of his express authority found in 11 U.S.C. § 704(a)(1).[1] According to the District Court, Code Section 704 only specifically authorized the Liquidation Trustee to collect property of the estate. Because the District Court concluded the assigned creditor claims were not property of the estate within the meaning of 11 U.S.C. § 541(a), it held the Liquidation Trustee had no statutory authority to bring suit. Ignoring *Sprint*, the District Court then concluded, based upon *Williams v. California 1st Bank*, 859 F.2d 664 (9th Cir. 1988), that this lack of express authorization in the Code coupled with the fact that the Trust would pay the proceeds of the assigned claims to the assigning creditors meant the Liquidation Trustee had no standing to prosecute the claims. (Pet. App. 17a-20a.)

The Seventh Circuit reversed, holding that under *Sprint* the Trust was the real party in interest with jurisdictional standing to prosecute the assigned claims even though it would pay any recoveries to the assigning creditors. (Pet. App. 2a-3a.) Having concluded that there was jurisdiction to allow an assignee, like the Trust, to pursue claims assigned to it for collection purposes, the Seventh Circuit reasoned that the issue before the Court was not one

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[1] The District Court's Opinion cites to section 704(1). (Pet. App. 16a.) Presumably this is a typographical error for there is no section 704(1). The correct citation is 11 U.S.C. § 704(a)(1).

of jurisdictional "standing" but rather whether the Trust had authority to prosecute the assigned claims. (Pet. App. 3a.)

On this point, the Seventh Circuit concluded that post-bankruptcy, the Bankruptcy Code did not govern the Trust or the permissible duties of the Liquidation Trustee; instead, the terms of the confirmed Plan and the Trust "govern the permissible duties of a trustee *after* bankruptcy." (Pet. App. 6a (emphasis in original).)

The Seventh Circuit then examined the three reasons set forth in *Caplin v. Marine Midland Grace Trust Co.*, 406 U.S. 416 (1972), for why a bankruptcy trustee should not be allowed to use section 70 of the former Bankruptcy Act (former 11 U.S.C. § 110; now 11 U.S.C. § 544) to prosecute claims belonging only to a subset of a debtor's creditors, and concluded that none of those reasons applied in this case to bar the post-confirmation Trust from prosecuting the claims assigned to it by its creditor-beneficiaries. (Pet. App. 6a-8a.) In reaching this conclusion, the Seventh Circuit noted that "the Bank's principal argument is that the Trust should not be allowed to deplete its assets by the expense of litigating the investor's claims." (Pet. App. 7a.) The Seventh Circuit rejected this argument both because this perceived harm does not injure the Bank and because no one, including the Bank, raised this objection before the Plan was confirmed, even though the alleged harm about which the Bank belatedly complained below "was apparent to any reader of the plan or the trust documents." (Pet. App. 7a.) Accordingly, the Seventh Circuit concluded that *Caplin* did not apply

and reversed the judgment of the District Court. (Pet. App. 8a.)

REASONS FOR DENYING THE PETITION

None of the three reasons the Bank offers in its Petition justify review of the Seventh Circuit's decision in this case. First, the Seventh Circuit's ruling does not conflict with this Court's decision in *Caplin v. Marine Midland Grace Trust Co.*, 406 U.S. 416 (1972), or with the Bankruptcy Code. Neither *Caplin* nor the Code addresses, let alone forbids the trustee of a post-bankruptcy trust established under state law from prosecuting creditors' claims assigned to that trust as the real party in interest. In fact, this Court already has spoken on this issue and opined to the contrary in *Sprint Communications Co., L.P. v. APCC Services, Inc.*, 554 U.S. 269, 128 S. Ct. 2531, 2536, 2542-43 (2008). There this Court held that an assignment of a cause of action provides the assignee with standing as the real party in interest to assert the claim even if the assignee is contractually obligated to pay all of the recoveries to the assignor. For this reason, the District Court was incorrect when it held that the standing issue was jurisdictional and prevented the Trust from proceeding on the assigned claims.

Second, the Seventh Circuit's ruling does not further deepen a Circuit split. The fact that the Seventh Circuit agreed with the Second Circuit and not the Ninth Circuit does not deepen a Circuit split where the decision the Seventh Circuit rejected, *Williams v. California 1st Bank*, 859 F.2d 664 (9th Cir. 1988), precedes *Sprint* by twenty years, is

distinguishable from the Seventh and Second Circuit decisions and is no longer good law following *Sprint*.

Third, the Seventh Circuit's ruling does not raise an important federal question that requires this Court's resolution. The Bank argues that this Court should intervene to prevent one group of the Trust's beneficiaries from potentially foisting their legal costs onto the other beneficiaries of the Trust. According to the Bank, this Court should step in to stop similar instances of "free riding." (Pet. 7.) An adequate mechanism, however, already exists to police the fairness of post-bankruptcy trusts. Under the Bankruptcy Code, creditors must vote to approve the terms of any chapter 11 plan that does not pay creditors in full. 11 U.S.C. §§ 1126, 1129(a)(10). If creditors believe that the terms of a post-confirmation trust are unfair or improvident, they can vote a plan down. The Court need not legislate protections beyond those already provided by the Bankruptcy Code, nor should it. Further, as the Seventh Circuit correctly observed, the Bank "is trying to fend off the Trust's claims not by standing on its own rights, but by asserting that the litigation might injure strangers (the Trust's beneficiaries). It's a basic principle that litigants can't invoke the rights of third parties." (Pet. App. 7a.)

Finally, review is inappropriate here for an additional reason. The Seventh Circuit concluded that the Bank's complaints were a collateral attack on a confirmed plan and therefore impermissible. (Pet. App. 7a-8a.) This ruling is in accord with this Court's recent decision in *United Student Aid Funds, Inc. v. Espinosa*, -- U.S. --, 130 S. Ct. 1367 (2010),

decided five days after the Seventh Circuit ruled in this case. There is no reason to revisit *Espinosa* given that this precedent is less than a year old and the case at bar does not raise any new points that would justify revisiting an issue so recently decided.

I. The Ruling Below Does Not Conflict With This Court's Rulings Or The Plain Meaning Of The Bankruptcy Code.

The Seventh's Circuit ruling does not conflict with this Court's precedent or federal law and, thus, there is no reason for the Court to review the lower court's decision. The Bank contends that the Seventh Circuit's decision is in conflict with this Court's ruling in *Caplin*, 406 U.S. 416. (Pet. 7-14.) *Caplin* held that a bankruptcy trustee appointed under chapter X of the now-repealed Bankruptcy Act did not have authority based upon section 70 of that Act (former 11 U.S.C. § 110) to bring suit on claims that belonged to a subset of the debtor's creditors, in that case, the debtor's bondholders. *Id.* at 434. Unlike the circumstances presented here, the bondholders in *Caplin* had not assigned their claims to the chapter X trustee. Instead, the chapter X trustee sought, on his own initiative, to pursue claims that belonged to third parties and that had not been assigned to the bankruptcy estate. *Id.* at 420. The chapter X trustee argued that the powers he held under section 70 were broad enough to create standing. *Id.* at 424-25.

This Court rejected this argument, noting that the Bankruptcy Act in effect at the time did not give the trustee the authority to bring claims that belonged to others. *Id.* at 432-34. In reaching this

conclusion, the Court set forth three reasons why it was appropriate to limit the use of section 70 in this manner. *Id.* The Court did not address what would have happened had the bondholders in *Caplin* actually assigned their claims to the chapter X trustee, and also did not discuss whether a post-bankruptcy successor to the debtor could accept assignments of such claims. *Id.*

In the Petition, the Bank makes much of the fact that when Congress enacted the current Bankruptcy Code it proposed a statutory provision that would have overruled *Caplin*, but ultimately did not include this provision in the Bankruptcy Code. The Bank argues that bankruptcy trustees receive no greater rights under the current Bankruptcy Code (11 U.S.C. § 544) than under former section 70. (Pet. 8.) The Trust, however, does not base its authority to sue the Bank on Code section 544 or on any other provision of the Bankruptcy Code; rather its authority to sue is based upon the terms of the confirmed Plan, the Trust and the voluntary assignments of those claims to the Trust. For this reason, the issue this Court decided in *Caplin* is not the same issue that the Seventh Circuit confronted below.

Instead, the Seventh Circuit considered whether the trustee of a trust created under state law -- not a trustee under either chapters 7 or 11 of the Bankruptcy Code -- has authority to prosecute claims as the assignee holding complete legal title to the assigned claims. As the decision below correctly recognizes, the Liquidation Trustee is not bound by *Caplin* but is pursuing those claims as the real party in interest, as did the assignee in *Sprint*.

Sprint held that an assignment of a cause of action provides the assignee with standing to assert the assigned claim even if the assignee is contractually obligated to pay all of the recoveries to the assignor. 128 S. Ct. at 2536, 2542-43. In *Sprint*, thousands of payphone operators assigned claims against the defendant long-distance communications carriers. *Id.* at 2534. Under the terms of the assignments, the aggregators agreed to "remit all proceeds" of the suits to the customers. *Id.* The petitioners argued that the aggregators lacked standing because they claimed to have suffered no injury themselves and would not retain any of the recoveries from the lawsuits. *Id.* at 2542. This Court rejected the argument that the assignments failed to convey standing to the assignee, and held that the aggregators could prosecute the assigned claims:

> [W]e have discovered that history and precedent are clear on the question before us: Assignees of a claim, including assignees for collection, have long been permitted to bring suit. A clear historical answer at least demands reasons for change. We can find no such reasons here, and accordingly we conclude that the aggregators have standing.

Id. at 2536.

Nor does the Bankruptcy Code limit the Liquidation Trustee's authority to prosecute the claims at issue here. Because the instant case has never been a chapter 7 case, section 704(a)(1) has never applied in this case. *See* 11 U.S.C. §§ 103(b),

1106(a). Thus, the District Court erred when it concluded that section 704(a)(1) placed a limit on what the Trust could do.

Instead, as the Seventh Circuit correctly held, the Bankruptcy Code not only permits, but expressly contemplates, that as part of a plan, a debtor may transfer estate property to a new entity charged with the responsibility for liquidating and distributing these assets to creditors. 11 U.S.C. § 1123(a)(5); *Holywell Corp. v. Smith*, 503 U.S. 47, 55 (1992); *Torch Liquidating Trust v. Stockstill*, 561 F.3d 377, 387 (5th Cir. 2009). The Bankruptcy Code places no limitation on the ability of such an entity to prosecute assigned creditor claims, and, indeed, places virtually no restrictions on the operations of such a liquidating entity post-confirmation. For this reason, no court has ever extended any of the standing restrictions or limitations imposed upon bankruptcy estates or bankruptcy trustees to a post-confirmation liquidation entity. The only other Court of Appeals to reach the issue, the Second Circuit, reached the same result as the Seventh Circuit, concluding that there is no prohibition upon a post-confirmation trust taking an assignment of creditor claims. *Semi-Tech Litig., LLC v. Bankers Trust Co.*, 450 F.3d 121, 126-27 (2d Cir. 2006), *adopting* 272 F. Supp. 2d 319, 324 (S.D.N.Y. 2003).

Thus, as the Seventh Circuit correctly recognized, "the terms of the Bankruptcy Code govern the permissible duties of a trustee *in* bankruptcy [and] the terms of the plan of reorganization (and of the trust instrument) govern the permissible terms of a trustee *after* bankruptcy." (Pet. App. 6a (emphasis

in original).) For this reason, the Seventh Circuit's opinion is not in conflict with federal law.

II. The Ruling Below Does Not Deepen A Circuit Split Over Trustee Standing Because After *Sprint*, *Williams* Is No Longer Good Law.

There also is no Circuit split on the question raised by the Bank's Petition for two reasons. First, as the Bank acknowledges, the Ninth Circuit's decision, *Williams,* 859 F.2d at 667, involves the ability of a chapter 7 trustee to prosecute an assigned cause of action. (Pet. 14.) Unlike the instant case, the trustee in *Williams* was not the trustee of a post-confirmation Trust. This distinction is critical because, as the Seventh Circuit explained in its ruling, the Trust is not governed by the Bankruptcy Code, but rather by the terms of the confirmed plan and the trust agreement. (Pet. App. 6a.)

Second, after *Sprint*, the rationale underlying the *Williams* decision is no longer good law. In *Williams*, the Ninth Circuit concluded that because the assignees of the claims would receive "the bulk of any recovery" collected by the chapter 7 trustee, they remained the "real parties in interest" on the assigned claims, not the chapter 7 trustee. 859 F.2d at 666-67. For this reason, the Ninth Circuit concluded that the trustee was not bringing claims on behalf of the estate.

Sprint, however, explicitly rejects the premise of *Williams*, holding that an assignee with complete legal title to the assigned claims is the real party in interest no matter how it will distribute the proceeds

of any recoveries. 128 S. Ct. at 2542-43. It is now settled, under *Sprint*, that an assignee is the real party in interest, irrespective of whether the assignee will receive a benefit from the litigation. *Id.* at 2544. As this Court held, "an assignee for collection may properly bring suit to redress injury originally suffered by his assignor." *Id.* at 2543.

Moreover, there is no prohibition in the Bankruptcy Code against a bankruptcy estate acquiring property post-petition through an assignment. 11 U.S.C. § 541(a)(7) expressly provides that property of the estate includes "[a]ny interest in property that the estate acquires after the commencement of the case." Therefore, if the Ninth Circuit were to revisit the issue it decided 22 years ago in *Williams,* it likely would conclude that because a chapter 7 trustee may acquire property post-petition, including causes of action, and because, if a trustee does so, under *Sprint,* the estate would be the real party-in-interest, no matter to whom it paid the recoveries, the holding in *Williams* is no longer good law.

The two cases the Bank highlights in its Petition certainly do not warrant this Court's review. They are not federal Court of Appeals decisions and both are distinguishable. In *Mukamal v. Bakes*, 383 B.R. 798 (S.D. Fla. 2007), the terms of the assignments purported to allow both the trust and the creditors to bring exactly the same claims. In particular, the plan expressly allowed the assignors/creditors "to initiate and pursue their own identical actions independent of litigation initiated by the [liquidation trustee], so long as their independent actions do not

seek the proceeds of the directors and officers insurance policies that cover the defendants." *Id.* at 813 n.13. Consequently, the purported assignments failed to transfer the assigned creditor claims exclusively to the liquidation trust. In addition, on grounds of untimeliness, the court did not allow the liquidation trustee to argue that the liquidating trust was created under state law rather than under the Bankruptcy Code. *Id.* at 811 n.9. Finally, the court recognized that the liquidation trustee might have had standing if all creditor claims had been assigned to him. *Id.* at 814.

In *Trenwick America Litigation Trust v. Ernst & Young*, 906 A.2d 168 (Del. Ch. 2006), *aff'd sub nom. Trenwick America Litigation Trust v. Billett*, 931 A.2d 438 (Del. 2007), the court found that the creditors had not assigned their claims to the litigation trustee and therefore he could not bring the claims. 906 A.2d at 189-191. The court's alternative ground for decision -- that the litigation trust would not have had standing under federal bankruptcy law even if the creditor claims had been assigned -- was pure dictum. *Id.* at 191.

In its ruling the Seventh Circuit carefully analyzed why *Caplin* was inapplicable and why it disagreed with *Williams*. But that decision ultimately does not matter because *Sprint* has already resolved any Circuit split that existed by knocking out the rationale of the *Williams* decision. Since neither *Caplin* nor the Bankruptcy Code forbid a state-law created post-bankruptcy trust from pursuing creditor claims assigned to it, this Court should deny the Bank's Petition.

III. The Ruling Does Not Raise An Important Federal Question That Requires This Court's Consideration Because The Bankruptcy Process Does Not Stand To Suffer Substantial Harm.

The Seventh Circuit's ruling does not threaten severe adverse practical consequences to pending bankruptcy cases. The Bank claims that if the Seventh Circuit's ruling is not reversed, trustees will not be able to resist drawing freely on estate assets to pursue creditor claims. According to the Bank, this creates two problems. First, creditors that participate in such trusts may be harmed if the litigation recoveries on account of assigned claims are not paid to them. (Pet. 17-19.) The Bank speculates that some creditors will be forced to subsidize the litigation costs of others. (*Id.*) Second, the Bank contends that the Seventh Circuit's ruling may allow bankruptcy trustees to run amok without any exercise of prudent litigation judgment. (*Id.*)

Both arguments are specious. As to the first, the Bankruptcy Code already puts in place adequate mechanisms to protect creditors. Under the Bankruptcy Code, creditors must vote to accept a chapter 11 plan that does not repay their claims in full. 11 U.S.C. §§ 1126, 1129(a)(10). If a plan prejudices creditors, they can vote against the plan and it will not be confirmed. 11 U.S.C. § 1129(a)(10). Further the bankruptcy court must find that any plan that is confirmed "has been proposed in good faith and not by any means forbidden by law." 11 U.S.C. § 1129(a)(3). These provisions of the Code already protect creditors adequately against unfair

plans. The Court should not impose a judicial solution for a problem that does not exist.

The underlying premise of the Bank's second argument is without merit. The Bank contends that trusts like the Trust are not constrained by litigation costs from bringing lawsuits based upon assigned claims. Thus, the Bank argues that without some form of constraint a trust will bring claims without regard to whether such claims have merit and entities like the Bank will be exposed needlessly to litigation risk. Existing procedures, however, protect the Bank against meritless litigation, including Fed. R. Civ. P. 11 and 28 U.S.C. § 1927.

Another important safeguard also exists to protect against improvident trustees. Presumably creditors (who want to receive payment on their claims) will not select a trustee who has failed to exercise prudent litigation judgment or who has run up expenses prosecuting meritless claims achieving limited or no results in his earlier cases. Thus, imprudent trustees will be weeded out of the process. Again, these protections sufficiently guard against the harms the Bank predicts from allowing creditors to assign their claims to a post-bankruptcy trust.

The Bank's proposed solution -- an outright ban forbidding post-bankruptcy trusts from pursuing assigned claims -- would deprive bankruptcy estates from the benefits that post-bankruptcy trusts create. As the Seventh Circuit recognized, such trusts serve the legitimate purpose of facilitating "efficient aggregation of claims." (Pet. App. 4a.) In this case, the assignment of creditor claims to the Trust has improved the Trust's ability to settle with third party

defendants other than the Bank. These settlements have achieved a greater recovery for the benefit of the creditor-beneficiaries of the Trust while providing the settling third-parties with broader releases. Trusts that provide for the assignment of creditor claims serve legitimate and important purposes.

IV. Further Review Is Not Warranted Because This Court Adequately Addressed The Question Presented Here In *Espinosa*.

One of the grounds for the Seventh Circuit's ruling below was that it was too late for the Bank to challenge the terms of the Trust. Relying upon decisions that hold that a plan of reorganization is not subject to collateral attack once it is confirmed, the Seventh Circuit held that even if the Bank had the right to complain about the terms of the Trust, it was too late for it to do so because the Plan had already been confirmed. (Pet. App. 7a-8a.)

This holding is in accord with this Court's decision in *Espinosa*, -- U.S. --, 130 S. Ct. 1367, decided five days after the Seventh Circuit ruled in this case. In *Espinosa*, a bankruptcy court confirmed a chapter 13 plan which provided that the debtor's student loans would be discharged even though such debts were not dischargeable under 11 U.S.C. § 1328. The creditor, however, did not object to the plan or appeal the confirmation order. Thereafter, the creditor challenged the order. The Court declined to void the confirmation order, concluding that even if the terms of the plan in that case were not consistent with the Bankruptcy Code, that did not make the

bankruptcy court's final judgment confirming the plan void. *Id.* at 1377.

Espinosa teaches that the time for the Bank to have raised its complaints about the Trust was during the confirmation hearing. Though it preceded *Espinosa*, the Seventh Circuit's decision also concluded that the Bank was too late to raise its "belated challenge to a confirmed plan of reorganization." (Pet. App. 8a.)

Espinosa has definitively answered, in the negative, whether a creditor can raise a challenge to the terms of a plan after the order confirming the plan has become a final order. Reviewing this case, which raises nearly the identical issue, will not further clarify or expand this rule of law. Therefore, there is no basis for this Court to review the Seventh Circuit's decision below.

CONCLUSION

For the foregoing reasons, this Court should deny the petition for writ of certiorari.

Respectfully submitted,

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In the Supreme Court of the United States

THE BANK OF NEW YORK MELLON AND
THE BANK OF NEW YORK MELLON CORPORATION,
Petitioners,

v.

FREDERICK J. GREDE, AS TRUSTEE OF THE
SENTINEL LIQUIDATION TRUST,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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As the petition demonstrates, the Seventh Circuit's ruling conflicts with *Caplin* v. *Marine Midland Grace Trust Co.*, 406 U.S. 416 (1972), deepens a circuit split over the scope of trustee litigation authority, and risks immense harm to the bankruptcy process. Grede offers no valid reason why the petition should not be granted.

1. Grede repeatedly contends that the question presented—whether a trustee appointed by a bankruptcy court to liquidate the estate has standing to sue third parties where any recovery will not go to the estate—is governed by *Sprint Communications Co.* v. *APCC Services, Inc.*, 128 S. Ct. 2531 (2008). But *Sprint* addresses a completely different question—whether an assignee has standing to sue where the proceeds will be passed on to the assignors. The issue here is not whether the proceeds will go to the assignors or the assignee, but whether they will go the estate.

That is the precise question addressed by this Court in *Caplin*. *Caplin* held that a trustee lacks authority to bring such suits, Congress reaffirmed the *Caplin* rule when it enacted the Bankruptcy Code in 1978, and the Ninth Circuit in *Williams* v. *California 1st Bank*, 859 F.2d 664 (9th Cir. 1988), held that the *Caplin* rule is not ousted merely because a liquidation trustee holds assigned claims. Grede's contention that *Sprint* limits *Caplin* and overrules *Williams* finds no support in *Sprint* (which does not address bankruptcy law, trustees, or estates) or in any court decision or secondary authority. Indeed, this Court in *Sprint* made clear that it was making no "change" to "history and precedent." 128 S. Ct. at 2536 (quoted at Opp. 13). That unchanged precedent must include *Caplin*.

2. Grede attempts to distinguish *Caplin* by contending that it has no application after a plan has been confirmed. But the liquidation trust established by the Plan here was simply a mechanism to liquidate the estate. Grede acknowledges (at 14) that if the bankruptcy court had administered the liquidation, the bankruptcy trustee would lack standing to bring a suit of this sort. There is no valid reason why the court's delegation of that task to a trust would abrogate the *Caplin* limit on trustee litigation authority. The Plan provided that "the Chapter 11 Case will remain open pending final order of the Bankruptcy Court closing the case and the Bankruptcy Court ***shall retain jurisdiction*** * * * to determine on a non-exclusive basis, any and all Causes of Action and Non-Estate Claims that have been transferred to the Litigation Trust." C.A. App. 104 § 9.1(b) (emphasis added). Thus, Grede as liquidation trustee continues to function under the oversight of the bankruptcy court and is not emancipated from the strictures of *Caplin*.

3. Grede offers no statutory support for his view that bankruptcy-court-appointed trustees may pursue litigation that will not benefit the estate. Yet it was the absence of such statutory support that led this Court in *Caplin* to conclude that trustees have no such authority. Grede attempts to limit the force of *Caplin* by suggesting (at 11) that it was construing the "now-repealed" Bankruptcy Act. But as Grede acknowledges (at 12), Congress expressly rejected a proposal to overrule *Caplin* and expand trustee litigation authority when it adopted the Bankruptcy Code in 1978. Congress thereby ensured that trustee litigation authority would continue to be limited to actions designed to benefit the estate. Although Grede (at 13-14) is correct that 11 U.S.C. § 704(a)(1)

does not expressly apply to Chapter 11 reorganizations, it is undeniable that a liquidating trustee has the duty to "collect and reduce to money the property of the estate," as § 704(a)(1) provides.

4. Grede asserts (at 15) that there is "no Circuit split" on the question presented. But the Seventh Circuit expressly noted that its ruling conflicts with the Ninth Circuit's decision in *Williams* and deepens an existing circuit split: "We must choose between the second circuit's holding and the ninth's." Pet. App. 5a. The Seventh Circuit sided with the Second Circuit against the Ninth Circuit, deepening a conflict that Grede cannot heal by speculating (at 16) that the Ninth Circuit today "likely would conclude [that] *Williams* is no longer good law." The Ninth Circuit has said nothing to undermine its *Williams* holding, and courts continue to cite it favorably. *E.g.*, *In re Bradley*, 326 F. App'x 838, 839 (5th Cir. 2009); *Charles Schwab & Co.* v. *Reaves*, 2010 WL 447370, at *4 (D. Ariz. Feb. 4, 2010).

Grede (at 16-17) attempts to distinguish two such cases cited in the petition, *Trenwick Am. Litig. Trust* v. *Ernst & Young, L.L.P.*, 906 A.2d 168 (Del. Ch. 2006), aff'd sub nom. *Trenwick Am. Litig. Trust* v. *Billett*, 931 A.2d 438 (Del. 2007), and *Mukamal* v. *Bakes*, 383 B.R. 798 (S.D. Fla. 2007), aff'd on other grounds, 2010 WL 1731775 (11th Cir. Apr. 30, 2010). But Grede disregards the *Trenwick* court's plain statement that "[t]he rule articulated in *Caplin* holds true even in cases where a creditor has assigned her claims to a trustee or Trust" (906 A.2d at 191), as well as the *Mukamal* court's conclusion that a post-confirmation liquidation trustee would lack standing to pursue assigned claims.

Grede suggests (at 17) that the *Mukamal* court's ruling would have been different "if all creditor claims" had been assigned to the trustee. But in that very different situation (not found in *Mukamal* or in this case), all estate creditors would share in the recovery and the *Caplin* issue would not arise. Grede (at 16) also derides both *Mukamal* and *Trenwick* as "not federal Court of Appeals decisions." But *Trenwick* was affirmed by Delaware's highest court, and *Mukamal* was affirmed by the Eleventh Circuit. Although the Eleventh Circuit's affirmance was based on other grounds, the court of appeals did not question the district court's view that the *Caplin* rule applies to a post-confirmation liquidation trustee holding assigned claims. See 2010 WL 1731775. These rulings exemplify the breadth of the division in the courts on the scope of the *Caplin* rule, confirming the need for this Court's review.

5. Grede contends (at 18-19) that the petition raises no important federal question because abrogation of the *Caplin* rule on trustee standing in this context does not risk practical harm to the bankruptcy process. But Grede does not contest that the ruling below allows *Caplin* to be circumvented by a mere formalistic recharacterization from bankruptcy trustee to liquidation trustee. Nor does he contest that this mere switch of hats lets the trustee draw freely on estate assets to pursue litigation that will not benefit the estate but only a subset of assigning creditors (and the trustee himself). Grede offers no statutory or policy defense for such forced litigation financing.

Instead, Grede argues (at 19) that application of the *Caplin* rule in this recurring context "would deprive bankruptcy estates from the benefits that post-

bankruptcy trusts create." That is not true at all. The Bank does not contest the use of liquidation trusts as a mechanism to liquidate estates, nor does it seek an "outright ban" on assignments to such trusts as Grede asserts (*ibid.*). The Bank contests only the authority of liquidation trustees to use estate assets to sue for recoveries that will not benefit the estate.

The Court in *Caplin* recognized the problems that such suits would generate, and Congress did as well when it refused to derogate from the *Caplin* rule in 1978. Grede's suggestion (*ibid.*) that Rule 11 and other protections against frivolous lawsuits would obviate these concerns is itself frivolous. *Caplin* did not address the merits of trustee lawsuits but rather the trustee's lack of statutory authority to file non-estate lawsuits and the conflicts and perverse incentives they would generate. As Judge Diane Wood has noted, a trustee's obligation to act "on behalf of the estate or the creditors as a whole" means that she "obviously may not roam around collecting whatever property suits her fancy." *Fisher* v. *Apostolou*, 155 F.3d 876, 880 (7th Cir. 1998). Yet that is the upshot of the ruling below, contrary to Congress's policy decisions to limit the litigation authority of trustees and to reject proposals to expand that authority.

Grede also argues (at 18) that estate creditors can prevent any harm from forced financing of litigation that will not benefit the estate by voting against or objecting to a plan that "does not repay their claims in full." But as in this case, creditors often have no idea what lawsuits a trustee may bring post-confirmation. Here, creditors had no reason to believe that Grede would not adhere to his legal responsibility to seek recoveries only for the estate (or Liquidation Trust). The remote possibility that

Grede might depart from that responsibility and bring suit where he would lack standing was far too hypothetical to sustain an objection or provide a reason to vote against the Plan. See *Holywell Corp.* v. *Smith*, 503 U.S. 47, 58 (1992) (rejecting contention that the United States, a creditor, "should have objected to the plan if it had wanted a different result" where the obligation of the trustee to file tax returns did not arise until after confirmation of the plan). Indeed, when confirmation of the Plan was being considered, the Trustee had already filed claims against the Bank in a prior lawsuit on behalf of the estate, and creditors had no reason to expect that the Trustee would file yet another action based on the same allegations.

6. For the same reason, Grede's preclusion argument (at 20-21)) is misplaced. Grede contends that the Bank's failure to object to the Plan's provision for assigning creditor claims to the Liquidation Trust precluded it from objecting to standing when this case was filed. But the issue here is not assignment but standing, which was not an issue before this case was filed well after confirmation of the Plan. Bankruptcy courts cannot decide issues "at a stage when they are not directly in issue and neither party has a full incentive to litigate them." *Brown* v. *Felsen*, 442 U.S. 127, 134 (1979). Standing cannot be addressed before a concrete case arises, and attempting to do so on a hypothetical basis would simply hamper the confirmation process and drain even more assets from the debtor's estate. As the district court explained, "[i]t is difficult to see how the issue of standing in this adversarial action could have been litigated as part of the less-formal confirmation process before the adversarial action itself was even filed." Pet. App. 13a.

Grede can obtain no support for his preclusion argument from *United Student Aid Funds, Inc.* v. *Espinosa*, 130 S. Ct. 1367 (2010). That case does not address whether a trustee's standing to bring a post-confirmation lawsuit must be determined prior to confirmation to avoid preclusion. In fact, it addresses only the narrow question of "whether an order that confirms the discharge of a student loan debt in the absence of an undue hardship finding or an adversary proceeding, or both, is a void judgment for Rule 60(b)(4) purposes." *Id.* at 1373. As with *Sprint*, Grede again relies on a case that does not answer the question presented.

7. In sum, Grede offers no viable reason for denying the petition. Mounting bankruptcies and the use of post-confirmation liquidation trusts have created incentives for trustee-initiated litigation that exceeds the limits prescribed by Congress and this Court. The ruling below gives judicial imprimatur to these unauthorized suits, risking great harm to the bankruptcy process and severe burdens on the federal judiciary. As this Court said in *Caplin*, the scope of trustee litigation authority is an important policy question best left to Congress.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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